SMART INVESTOR

Keep and Grow Your Money

N. Mario Cerutti

For Petra, who reminded me to do this.

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N. Mario Cerutti

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Contents Overview

Contents Detailed

Preface

Reference

0-1 Significance of AI in the Personal Investment Universe

Chapter 1 Why Investing?

Chapter 2 Avenues to Invest

Chapter 3 The Markets

Chapter 4 Rules of Investing

Chapter 5 How to Engage

Chapter 6 Portfolio Models

Chapter 7 Management

Index

Contents Detailed

Preface

Reference

0-1 Significance of AI in the Personal Investment Universe

Chapter 1 Why Invest?

1-1 The Trap of Cash

1-11 Your Cash Under the Mattress

1-12 What Is Inflation?

1-13 History of Inflation

1-14 The Importance of Investing

Chapter 2 Avenues to Invest

2-1 Asset Allocation

2-11 Definition

2-12 Asset Classes

2-121 FOREX

Chapter 3 The Markets

3-1 Stocks

3-11 Definition

3-12 Size

3-13 Evaluation

3-2 Bonds

3-21 Definition

3-22 Size

3-23 Evaluation

3-3 Real Estate

3-31 Definition

3-32 Size

3-33 Evaluation

3-4 Commodities

3-41 Definition

3-42 Size

3-43 Evaluation

3-44 Gold

3-441 Definition

3-442 Size

3-443 Evaluation

3-5 FOREX

3-51 Definition

3-52 Size

3-53 Evaluation

3-6 Alternatives

3-61 Hedge Funds

3-611 Definition

3-612 Size

3-613 Evaluation

3-62 Private Equity

3-621 Definition

3-622 Size

3-623 Evaluation

3-63 Venture Capital

3-631 Definition

3-632 Size

3-633 Evaluation

3-7 Collectibles

3-71 Definition

3-72 Size

3-73 Evaluation

3-8 Crypto

3-81 Definition

3-82 Size

3-83 Evaluation

3-9 Comparison

Chapter 4 Rules of Investing

4-1 Golden Rules

4-11 Liquidity

4-12 Diversification

4-13 Performance

4-14 Risk

4-15 Time

4-16 Goals

4-17 Costs

4-18 Consistency

4-19 Simplicity

4-2 Putting It All Together

4-21 Investment Pyramid

4-22 Decision Tree

4-23 Checklist

Chapter 5 How to Engage

5-1 Day Trading

5-2 Stock Picking

5-3 Market Timing

5-4 Derivatives

5-5 Robo Investing

5-6 Funds

5-61 Mutual Funds

5-62 ETF

5-63 Managed Funds

5-54 Index Funds

Chapter 6 Portfolio Models

6-1 Definition

6-2 Strategies

6-3 Keep It Simple

6-31 The Long-Term Approach

6-311 Stocks Beat Them All

6-312 Diversification Helps

6-32 One Asset

6-33 Two Assets

6-34 Three Assets

6-35 Four Assets

6-36 Five Assets

6-37 Six Assets

6-4 More Portfolio Models

Chapter 7 Management

7-1 Account

7-2 Monitoring

Index

Preface

The significance of artificial intelligence (AI) in the investment universe is already profound and growing rapidly. As a case study, the parameters (framework, focus, and thrust) of this eBook have been set up by the author. The headings appear in blue, and the text following the headings was created with AI assistance. The results have been backtested to ensure accuracy. The author's creative vision and profound expertise in Investment Management have guided this endeavor

S. G.

Reference

OpenAI. (2025). ChatGPT (4.0) [Large language model]. https://chat.op

0-1 Significance of AI in the Personal Investment Universe

Artificial Intelligence (AI) is revolutionizing how individuals invest, transforming the landscape with smarter, faster, and more accessible tools. From personalized strategies to real-time risk monitoring, AI is empowering investors at every level to make more informed and tailored financial decisions.

Personalized Investment Strategies

AI-driven platforms assess individual investor profiles, including goals, risk tolerance, and spending behavior. This allows for customized asset allocation and dynamic portfolio rebalancing. Whether for retirement, income generation, or long-term growth, AI helps deliver optimized strategies that evolve with the investor.

The Rise of Robo-Advisors

Robo-advisors, powered by AI, have democratized financial planning. Services such as Betterment and Wealthfront offer low-cost investment management, goal-based tracking, and tax-loss harvesting. These platforms make professional-grade financial advice accessible to retail investors.

Real-Time Risk Assessment

AI continuously monitors market volatility, credit risk, and macroeconomic trends using tools like natural language processing (NLP) and machine learning. Investors benefit from proactive alerts and scenario-based stress testing, leading to improved drawdown management and capital preservation.

Fraud Detection and Cybersecurity

AI enhances security by detecting anomalies in account activity, identifying fraudulent transactions, and providing real-time alerts. As more investing takes place online and via mobile apps, this layer of protection is essential to safeguard personal assets.

Sentiment and Behavioral Analysis

AI systems analyze news, social media, and analyst reports to gauge market sentiment. By identifying hype cycles and psychological trends, investors can better time trades and manage behavioral biases in decision-making.

Algorithmic and Quantitative Trading

AI makes advanced trading strategies available to retail investors through bots and smart algorithms. These systems use reinforcement learning and predictive modeling, enabling individuals to mirror the tactics of institutional hedge funds.

Conversational Interfaces

AI-powered tools like ChatGPT simplify complex financial research and analysis. Investors can query markets, interpret earnings reports, and receive portfolio advice in plain language, improving accessibility and financial literacy.

Predictive Analytics

AI forecasts stock movements, economic indicators, and earnings surprises. Integrated into investment apps and screeners, these predictive models guide better decision-making and help investors anticipate opportunities and risks.

Cost Reduction and Accessibility

AI significantly lowers the cost of investment services. It enables fractional investing, automates routine advisory tasks, and operates around the clock, extending professional support to those with modest capital.

Integration with Emerging Technologies

AI synergizes with blockchain for secure asset management, with IoT for real-time ESG data, and with AR for interactive financial planning tools. These integrations are pushing the boundaries of what's possible in personal investing.

Challenges and Caveats

Despite its advantages, AI presents challenges:

- Models can overfit and produce misleading results.
- Biases in training data may reinforce inequality.
- Black-box algorithms reduce transparency.
- Over-reliance may impair critical thinking.

Final Thought

AI is a powerful tool that enhances—rather than replaces—the timeless principles of investing:

- Liquidity, Diversification, Performance
- Risk Management, Time, Goals
- Costs, Consistency, Simplicity

When used thoughtfully, AI can help investors navigate complexity and build resilient, purpose-driven portfolios for the future.

Chapter 1

Why Invest?

1-1 The Trap of Cash

1-11 Your Cash Under the Mattress

If you had left USD 10,000 under a mattress 100 years ago (in 1925) and retrieved it in 2025, its nominal value would still be $10,000, but its purchasing power would have drastically diminished due to inflation.

Adjusted for Inflation:

Using U.S. inflation data, $10,000 in 1925 is equivalent to approximately: $175,000 – $180,000 in 2025 dollars

This means:

- **Lost purchasing power**: Your $10,000 would buy today only a small fraction of what it could in 1925.
- **Real value today**: That money has lost over 94% of its value due to inflation.

How this is calculated:
The U.S. average annual inflation rate over the past 100 years has been about 3%. Compounded over a century, that erodes value significantly.

Investing that $10,000 in the S&P 500 (with dividends reinvested) instead might have grown to over $100 million depending on the exact dates and compounding assumption. Let's compare what happened to $10,000 left under a mattress vs. $10,000 invested in the S&P 500 from 1925 to 2025:

$10,000 Under the Mattress (1925–2025)

- Nominal value: Still $10,000
- Inflation-adjusted (2025): Worth about $175,000–$180,000
- Effective return: -94% real value loss
- Conclusion: Safe from market risk, but crushed by inflation.

$10,000 Invested in the S&P 500 (with dividends reinvested)

The S&P 500 (or a similar index like the Composite Index pre-1957) has returned an average of ~10% annually, including dividends, over the last 100 years.

Using that:

➤ Future Value Formula**:** $FV = 10{,}000 \times (1 + 0.10)^{100}$

$10,000 in 1925 could grow to ~$137.8 million by 2025

(assuming consistent reinvestment, no taxes or fees).

Comparison Summary

Strategy	2025 Value	Notes
Mattress	**~$10,000**	**Lost ~94% of purchasing power**
Adjusted for Inflation	**~$175,000**	**Equivalent value in 2025 terms**
Invested in S&P 500	**~$137.8 million**	**Power of compounding over a century**

Bottom Line:

Time and compound interest are a powerhouse duo. Hiding money in a mattress = safety but guaranteed loss of real value. Investing = volatility but massive long-term gains.

1-12 What Is Inflation?

Inflation is the rate at which the general level of prices for goods and services rises over time, which causes the purchasing power of money to decrease.

Key Points About Inflation

- **1. Price Increase**

  Over time, most goods and services become more expensive. For example:
  - A loaf of bread that cost $0.10 in 1925 might cost $3.00 today.
- **2. Decline in Money Value**

  The same amount of money buys fewer goods:
  - $100 today buys less than it did 20 years ago.
- **3. Measured as a Percentage**

  Inflation is usually expressed as an annual percentage:
  - If inflation is 3%, a $1.00 item will cost $1.03 next year.
- **4. Tracked by Indexes**

  Economists use indexes to measure inflation, such as:
  - CPI (Consumer Price Index)
  - PCE (Personal Consumption Expenditures)

Simple Example

Let's say inflation averages 3% per year.

- Year 1: An item costs $100
- Year 2: The same item costs $103
- Year 3: The same item costs $106.09

This compounding effect makes inflation add up over time.

Types of Inflation

- Creeping Inflation: Low and steady (e.g. 1–3% annually)
- Walking Inflation: Moderate (e.g. 3–10%)
- Galloping Inflation: High and fast (double digits)
- Hyperinflation: Extremely rapid (e.g. prices double in days or weeks)

Causes of Inflation

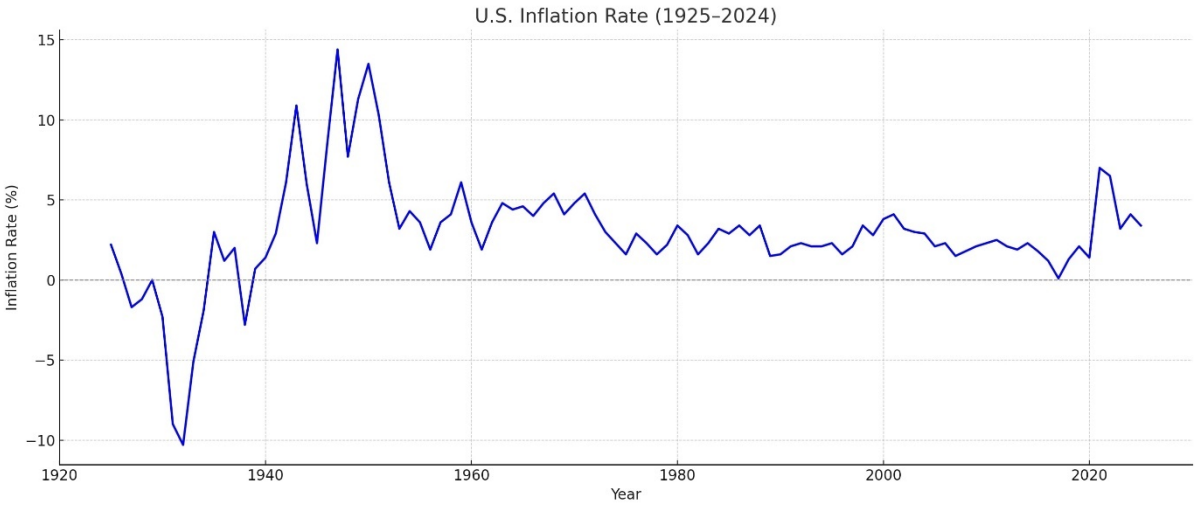
1. **Demand-Pull Inflation**
    - Too much money chasing too few goods.
    - Example: Increased consumer demand boosts prices.
2. **Cost-Push Inflation**
    - Rising costs of production (e.g., wages, materials).
    - Companies pass those costs to consumers.
3. **Built-In Inflation**
    - Workers demand higher wages → companies raise prices → cycle continues.

Why Inflation Matters

- Reduces the value of savings over time.
- Affects interest rates and wages.
- Central banks (like the Federal Reserve) manage it using monetary policy.

1-13 History of Inflation

Here is a visual chart showing the U.S. inflation rate from 1925 to 2024. This timeline reflects key economic events:



Notable Inflation Periods:

- 1930s (Great Depression): Deflationary years (negative inflation)
- 1940s (WWII): Inflation spikes due to war spending
- 1970s–early 1980s: High inflation era (energy crisis, wage-price spirals)
- 1990s–2010s: Relatively stable, low inflation
- 2021–2022: Post-COVID spike in inflation

Here's a breakdown of U.S. inflation across the last 100 years by decade, along with key historical events that influenced inflation in each period:

1920s–1930s: Volatility and Depression

Average Inflation: ~-2% (1930s), Low to Moderate (1920s)

- Events:
    - 1929: Stock market crash → Great Depression
    - 1930s: Massive deflation, prices dropped for years
- Impact: People delayed spending; deflation worsened the economic slump.

1940s: WWII and Wartime Economy

Average Inflation: ~5–6%

- Events:
    - WWII: Government ramped up spending, rationing
    - Post-war boom: Pent-up demand after wartime austerity
- Impact: Inflation surged as demand outpaced supply.

1950s: Post-War Stability

Average Inflation: ~2%

- Events:
    - Return to peacetime economy
    - Moderate growth, strong manufacturing
- Impact: Stable prices, solid consumer confidence.

1960s: Start of Inflation Pressure

Average Inflation: ~3%

- Events:
    - Vietnam War + Great Society spending
    - Expanding money supply
- Impact: Inflation crept up toward decade's end.

1970s: Stagflation Era

Average Inflation: ~7%

- Events:
    - 1973 and 1979 oil shocks: OPEC oil embargo, Iran Revolution
    - Wage-price spirals
    - Low economic growth + high inflation = stagflation
- Impact: Public trust in economic policy declined; interest rates soared.

1980s: Volcker Shock and Disinflation

Average Inflation: ~5.5% early, ~3% late

- Events:
    - Fed Chair Paul Volcker raised interest rates dramatically to fight inflation
    - Recession in early 1980s, recovery later
- Impact: Inflation tamed, but at cost of high unemployment early on.

1990s: Goldilocks Economy

Average Inflation: ~2.9%

- Events:
    - Tech boom, globalization, falling commodity prices
- Impact: Strong growth with low inflation and unemployment.

2000s: Recession and Recovery

Average Inflation: ~2.5%

- Events:
    - Dot-com bubble burst (2000)
    - 2008: Global Financial Crisis
- Impact: Temporary deflation in 2009, followed by modest inflation.

2010s: Low Inflation Era

Average Inflation: ~1.8%

- Events:
    - Post-2008 recovery, low interest rates
    - Quantitative easing (QE), yet inflation remained subdued
- Impact: Fed aimed for 2% but often fell short.

2020s (so far): Pandemic and Price Surge

Average Inflation (2020–2024): ~4.6%

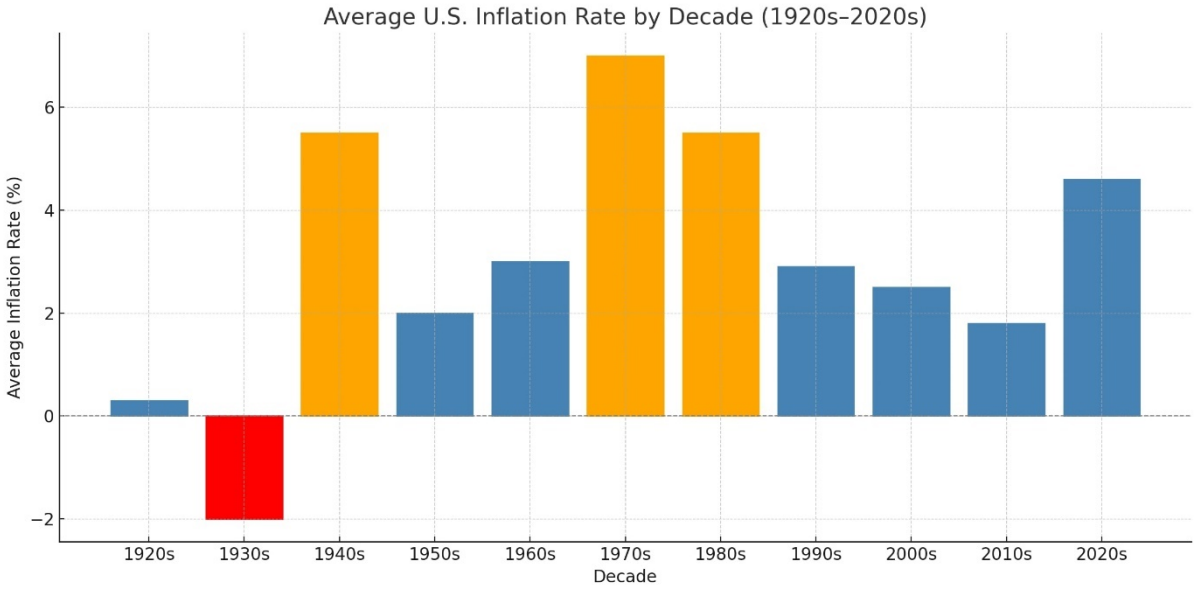
- Events:
    - 2020: COVID-19 lockdowns and supply chain disruption
    - 2021–2022: Inflation spike (up to 7–9%)
    - Fed hikes interest rates sharply in 2022–2023
- Impact: Cost of living jumped; mortgage and loan rates surged.

Summary Table

Decade	Avg. Inflation (%)	Key Events
1920s	~0.3	Roaring 20s, pre-crash boom
1930s	~-2.0	Great Depression (deflation)
1940s	~5.5	WWII, post-war demand
1950s	~2.0	Economic expansion, stability
1960s	~3.0	Vietnam War, government spending
1970s	~7.0	Oil crises, stagflation
1980s	~5.5	Fed hikes, disinflation
1990s	~2.9	Tech boom, globalization
2000s	~2.5	Dot-com crash, 2008 recession
2010s	~1.8	QE, low inflation
2020s*	~4.6	COVID-19, supply shocks

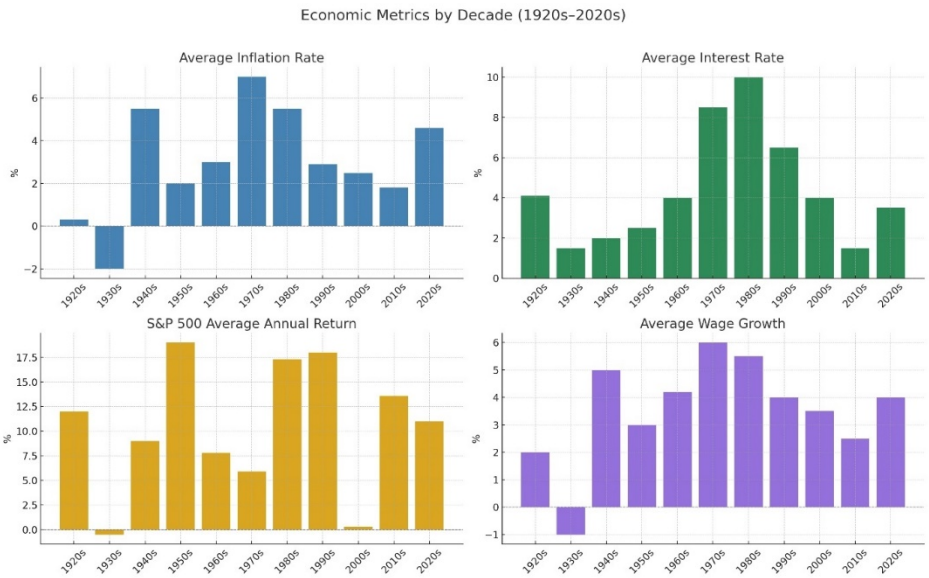
Visual bar chart showing the average U.S. inflation rate by decade from the 1920s to the 2020s.

- Red: Deflation (1930s)
- Orange: High inflation decades (1940s, 1970s, 1980s, 2020s)
- Steel blue: Moderate or low inflation decades



Multi-panel chart comparing four key economic indicators by decade:

1. Average Inflation Rate – Shows how the cost of living changed.
2. Average Interest Rate – Reflects borrowing costs and Fed policy trends.
3. S&P 500 Annual Return – Demonstrates long-term investment growth.
4. Average Wage Growth – Measures how worker income kept up with inflation.



Key Insights:

- 1970s–1980s: High inflation and interest rates, but moderate wage growth.
- 1990s: Strong stock returns with stable inflation and healthy wages.
- 2010s: Low inflation and interest rates, but stock returns remained high.
- 2020s: Inflation and rates rose sharply post-COVID, but wages lag behind.

1-14 The Importance of Investing

Why You Should Invest Instead of Saving Cash Under a Mattress:

1. Inflation Eats Away at Value

- Inflation reduces what your money can buy.
- Example: $1 in 1925 ≈ $17.50 today — that's over 94% loss in purchasing power.
- Cash under the mattress earns 0%, but prices keep rising.

2. You Miss Out on Compound Growth

- Investing allows your money to earn returns on returns (compounding).
- $10,000 invested in the S&P 500 over 100 years could become $130+ million.
- Under the mattress? Still $10,000 — minus buying power.

3. No Passive Income

- Investments like stocks, bonds, and real estate can pay:
    - Dividends
    - Interest
    - Rental income
- Cash sitting idle earns nothing.

4. Security Risks

- Stashing cash at home is risky:
    - Fire, theft, flood = total loss.
    - No FDIC insurance, no recovery options.

5. Opportunity Cost

- By not investing, you lose potential gains:
    - Markets historically return 6–10% annually (stocks)
    - Bonds and real estate also grow over time.
    - Mattress money = missed wealth building.

6. Your Money Won’t Work for You

- Investing is how you make your money work while you sleep.
- Cash under the mattress means you work for your money forever.

Example: 20-Year Comparison

Option	Annual Return	Value After 20 Years (Starting with $10,000)
Mattress	0%	$10,000 (worth less in real terms)
Savings Account	~1%	~$12,200 (barely beats inflation)
S&P 500 (avg return)	~10%	~$67,000+

Conclusion

Putting your money under a mattress feels “safe,” but it’s actually guaranteed loss in the long run. Investing intelligently is how you protect, grow, and build wealth over time.

Chapter 2

Avenues to Invest

2-1 Asset Allocation

2-11 Definition

In the investment world, Asset Allocation refers to the strategic distribution of an investor's portfolio across different asset classes to balance risk and reward according to goals, time horizon, and risk tolerance.

Definition:

Asset allocation is the process of dividing investments among different categories such as stocks, bonds, real estate, and cash to optimize returns and manage risk.

Key Components of Asset Allocation

1. **Asset Classes Typically Used:**
    - Equities (Stocks): Higher risk, higher potential return.
    - Fixed Income (Bonds): Lower risk, income-producing.
    - Cash or Cash Equivalents: Very low risk, minimal return.
    - Alternative Investments: Real estate, commodities, crypto, private equity, etc.
2. **Purpose:**
    - Diversify risk — different assets perform differently under various market conditions.
    - Align with personal investment goals and financial timeline.
3. **Types of Asset Allocation Strategies:**
    - Strategic Allocation: Long-term, fixed percentages (e.g., 60% stocks, 40% bonds).
    - Tactical Allocation: Adjusts based on short-term market opportunities.
    - Dynamic Allocation: Continuously adjusts based on economic conditions or personal circumstances.
    - Target-Date Funds: Automatically rebalance based on time to retirement.

Example of a Simple Portfolio:

Asset Class	Allocation	Description
Stocks	60%	Growth engine of the portfolio
Bonds	30%	Income and stability
Cash	10%	Liquidity and safety buffer

Why It Matters:

- Studies show asset allocation decisions account for 80–90% of a portfolio's long-term performance.
- Picking individual stocks or timing the market is far less impactful than having a well-balanced asset mix.

2-12 Asset Classes

The classical (or traditional) asset classes are the core categories of investments used in most portfolios to diversify risk and achieve specific financial goals.

The 4 Classical Asset Classes

1. Equities (Stocks)

- What: Ownership in a company (public or private).
- Returns: Capital appreciation + dividends.
- Risk/Reward: High potential return, high volatility.
- Examples:
    - U.S. or international stocks
    - Large-cap, small-cap, emerging markets

2. Fixed Income (Bonds)

- What: Loans to governments or corporations, paid back with interest.
- Returns: Interest income (called "yield").
- Risk/Reward: Lower risk than stocks, but lower returns.
- Examples:
    - U.S. Treasury bonds
    - Municipal bonds
    - Corporate bonds
    - Bond funds or ETFs

3. Cash and Cash Equivalents

- What: Liquid, short-term, low-risk investments.
- Returns: Minimal (often below inflation).
- Risk/Reward: Very low risk, but limited growth.

- Examples:
    - Physical cash
    - Money market accounts
    - Treasury bills (T-bills)
    - Certificates of deposit (CDs)

4. Real Assets (Tangible Assets)

- What: Physical items that have intrinsic value.
- Returns: Appreciation, rental income, or inflation protection.
- Risk/Reward: Moderate to high, depends on the asset.
- Examples:
    - Real estate (residential or commercial)
    - Commodities (gold, oil, agricultural goods)
    - Infrastructure (toll roads, utilities)

Optional (Sometimes Considered "Modern" Asset Classes)

Category	Included Assets
Alternatives	Hedge funds, private equity, venture capital
Cryptocurrencies	Bitcoin, Ethereum, other digital tokens
Collectibles	Art, wine, rare coins, luxury items

Summary Table

Asset Class	Return Potential	Risk Level	Liquidity	Income Generation
Equities	High	High	High	Possible (dividends)
Bonds	Moderate	Low–Medium	Medium	Yes (interest)
Cash	Low	Very Low	Very High	Minimal
Real Assets	Moderate–High	Medium	Low–Medium	Yes (rent, etc.)

2-121 FOREX

Is Forex (Foreign Exchange) an Asset Class? Technically, no — Forex is not a traditional asset class. It's more accurately considered a market or a trading instrument rather than a standalone asset class.

Explanation:

What Forex Is:

- Forex (foreign exchange) is the market for trading currencies.
- Example: USD/EUR, GBP/JPY, etc.
- It's the largest and most liquid market in the world.

Why It's Not a Standalone Asset Class:

- Currencies are not income-generating (they don't pay dividends or interest unless tied to interest rate differentials).
- They don't have intrinsic value like stocks, bonds, or real estate.
- Currency values are relative, always compared to another currency.

Forex can be used as part of an investment strategy through:

1. Speculation – Trying to profit from currency movements.
2. Hedging – Protecting against currency risk (e.g., for international investors).
3. Diversification – Some investors treat currencies as alternative assets to reduce exposure to traditional market cycles.

So Where Does Forex Fit?

Category	**Considered As…**
Traditional Asset Class	No
Trading Instrument	Yes
Part of Alternatives	Sometimes (for speculators/hedgers)
Diversification Tool	Yes (especially for global investors)

Summary:

Forex is not a classical asset class like stocks, bonds, or real estate. But it's a powerful tool for trading, hedging, and global diversification.

Chapter 3

The Markets

3-1 Stocks

3-11 Definition

The stock market is a marketplace where shares of publicly traded companies are bought and sold. It provides a platform for investors to trade ownership stakes (called stocks or equities) in companies, and for businesses to raise capital by issuing shares to the public.

More formally: The stock market is a collection of markets and exchanges where regular activities of buying, selling, and issuing shares of publicly held companies take place.

The stock market is a system of interconnected exchanges and markets where investors can buy and sell shares (also called stocks) of publicly traded companies. It plays a central role in the global financial system, enabling companies to raise money and giving investors the opportunity to earn returns on their capital.

Key Components:

1. **Stocks (Shares):**
   These represent partial ownership in a company. When you own a stock, you own a "share" of that business and may be entitled to dividends and voting rights.
2. **Public Companies:**
   Companies list (or "go public") on the stock market through an Initial Public Offering (IPO), allowing the public to buy shares.
3. **Exchanges:**
   These are physical or digital platforms where stocks are traded.
   Examples:
   - New York Stock Exchange (NYSE)
   - NASDAQ
   - London Stock Exchange (LSE)
   - Tokyo Stock Exchange (TSE)
4. **Investors:**
   - Retail investors: everyday people investing for personal wealth.
   - Institutional investors: banks, hedge funds, pension funds, etc.
5. **Stockbrokers & Trading Platforms:**
   Middlemen or tools that help investors access the stock market (e.g., Robinhood, E*TRADE, Charles Schwab).

Purpose of the Stock Market:

- **For Companies:**
  Raise capital to fund growth, innovation, and operations.
- **For Investors:**
  Buy shares with the hope that their value will increase (capital gains), or earn income through dividends.
- **For the Economy:**
  A barometer of economic health — when stock markets rise, it's often seen as a sign of economic confidence.

How It Works:

- **Supply and Demand:** Stock prices move based on how much buyers are willing to pay and how much sellers want in return.
- **Market Orders & Limit Orders:** Investors can buy/sell at current market prices or set specific prices at which they're willing to trade.
- **Regulation:** Most markets are overseen by regulatory bodies (e.g., the U.S. SEC) to ensure fair and transparent trading.

3-12 Size

As of 2023, the global stock market had a total market capitalization of approximately $124.63 trillion. Statista

Geographical Distribution:

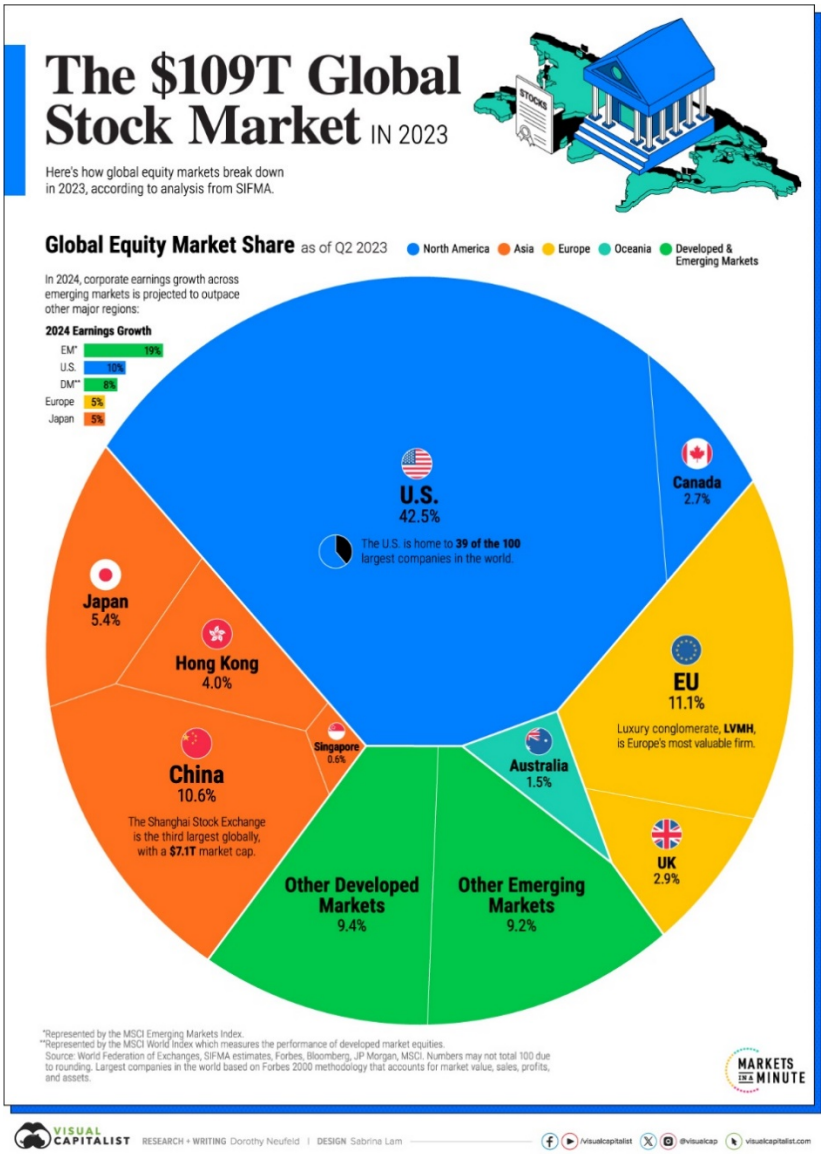
- **Americas:** Dominating the global market, the Americas' domestic equity market capitalization surged from $28.3 trillion in 2013 to $54.6 trillion in 2023.
- **Asia-Pacific (APAC):** This region accounted for 30% of the global market capitalization by the end of Q3 2023.
- **Europe, Middle East, and Africa (EMEA):** Collectively, these regions represented 23% of the global market capitalization at the end of Q3 2023. Statista focus

Top 10 Countries by Stock Market Capitalization Wikipedia

Rank	Country	Market Cap (USD Trillions)	% of Global Market Cap
1	United States	56.5	45.33
2	China	14.4	11.55

3	Japan	5.50	4.41
4	Hong Kong	5.46	4.38
5	India	5.06	4.06
6	Canada	3.46	2.77
7	France	3.45	2.76
8	United Kingdom	3.04	2.43
9	Saudi Arabia	2.69	2.15
10	Germany	2.18	1.74

These figures underscore the significant concentration of market capitalization in a few leading countries, with the United States holding a substantial share of the global equity market.


The $109T Global Stock Market IN 2023
Here's how global equity markets break down in 2023, according to analysis from SIFMA.
Global Equity Market Share as of Q2 2023
North America
Asia
Europe
Oceania
Developed & Emerging Markets
In 2024, corporate earnings growth across emerging markets is projected to outpace other major regions:
2024 Earnings Growth
EM* 19%
U.S. 10%
DM** 8%
Europe 5%
Japan 5%
U.S. 42.5%
The U.S. is home to 39 of the 100 largest companies in the world.
Canada 2.7%
EU 11.1%
Luxury conglomerate, LVMH, is Europe's most valuable firm.
UK 2.9%
Australia 1.5%
Singapore 0.6%
Japan 5.4%
Hong Kong 4.0%
China 10.6%
The Shanghai Stock Exchange is the third largest globally, with a $7.1T market cap.
Other Developed Markets 9.4%
Other Emerging Markets 9.2%
*Represented by the MSCI Emerging Markets Index.
**Represented by the MSCI World Index which measures the performance of developed market equities.
Source: World Federation of Exchanges, SIFMA estimates, Forbes, Bloomberg, JP Morgan, MSCI. Numbers may not total 100 due to rounding. Largest companies in the world based on Forbes 2000 methodology that accounts for market value, sales, profits, and assets.
MARKETS IN A MINUTE
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RESEARCH + WRITING Dorothy Neufeld | DESIGN Sabrina Lam
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3-13 Evaluation

Evaluation of the stock market as an investment option, across key dimensions that matter for individual or institutional investors:

1. Liquidity

Rating: ★★★★★ (High)

- Explanation: Major stock markets (like the NYSE, Nasdaq, London Stock Exchange, etc.) are highly liquid, meaning you can typically buy or sell shares quickly without affecting the price much.
- Blue-chip stocks (large, established companies) offer the greatest liquidity.
- Smaller or emerging market exchanges may have lower liquidity, which can lead to price slippage or wider bid-ask spreads.

2. Risk

Rating: ★★★★☆ (Moderate to High)

- Market Risk: Stock prices are volatile and influenced by macroeconomic factors, corporate performance, interest rates, and geopolitical events.
- Sector/Company Risk: Individual stocks can crash even when the broader market is rising.
- Currency Risk: For foreign investors, currency fluctuations can impact returns.
- Systemic Events: Crashes, bubbles (like 2008 or COVID-19 shocks), or flash crashes are always possibilities.

Mitigation: Diversification (via ETFs, mutual funds) and long-term holding strategies reduce risk.

3. Performance

Rating: ★★★★☆ (Historically Strong)

- Historical Returns:
    - U.S. stock market (S&P 500) has returned ~7–10% annually after inflation over long periods.
    - Emerging markets and tech-heavy indexes may offer higher growth, but with higher volatility.
- Growth Potential: Especially strong in sectors like tech, green energy, AI, and biotech.

Caveat: Past performance is no guarantee of future results, and timing matters (e.g., entering before a crash).

4. Costs (Entry/Exit for Investors)

Rating: ★★★★★ (Low, especially for retail investors)

- Brokerage Fees:
    - Most online brokers now offer zero-commission trades on stocks and ETFs in major markets.
- Bid-Ask Spread: Generally tight in liquid markets; wider in small-cap or emerging markets.
- Taxes:
    - Capital gains taxes apply on profits.
    - Dividend taxes vary by country and investor residency.
- Currency Conversion Fees: May apply for foreign investors.

Institutions may face exchange fees, custody fees, and regulatory costs, but these are typically manageable.

Summary Evaluation for Investors

Factor	Evaluation
Liquidity	★★★★★ Extremely high in major markets
Risk	★★★★☆ Volatile, mitigable with diversification
Performance	★★★★☆ Historically strong returns
Costs	★★★★★ Low for most retail investors

3-2 Bonds

3-21 Definition

The bond market, also known as the debt market or fixed-income market, is the financial market where participants issue, buy, and sell debt securities—primarily bonds.

What is a Bond?

A bond is a loan made by an investor to a borrower (typically a corporation, municipality, or government). In return, the borrower agrees to:

- Pay interest (called a coupon) at regular intervals.
- Repay the principal (the original loan amount) at the bond's maturity date.

Purpose of the Bond Market

- Governments use it to raise funds for public spending (e.g., infrastructure).
- Corporations use it to finance expansion, operations, or acquisitions—without giving up ownership (as with stocks).
- Investors use it for income and diversification, especially in low-risk portfolios.

Key Segments of the Bond Market

1. **Government Bonds**
    - Examples: U.S. Treasuries, UK Gilts, Japanese Government Bonds (JGBs)
    - Generally low-risk
2. **Corporate Bonds**
    - Issued by companies
    - Vary in risk and return based on the issuer's creditworthiness
3. **Municipal Bonds (Munis)**
    - Issued by states, cities, or local authorities
    - Often tax-exempt (in the U.S.)
4. **Supranational Bonds**
    - Issued by institutions like the World Bank or European Investment Bank

In Simple Terms:

The bond market is where governments and companies borrow money from investors, promising to pay it back later with interest.

3-22 Size

As of 2023, the global bond market was valued at approximately $135 trillion. S&P

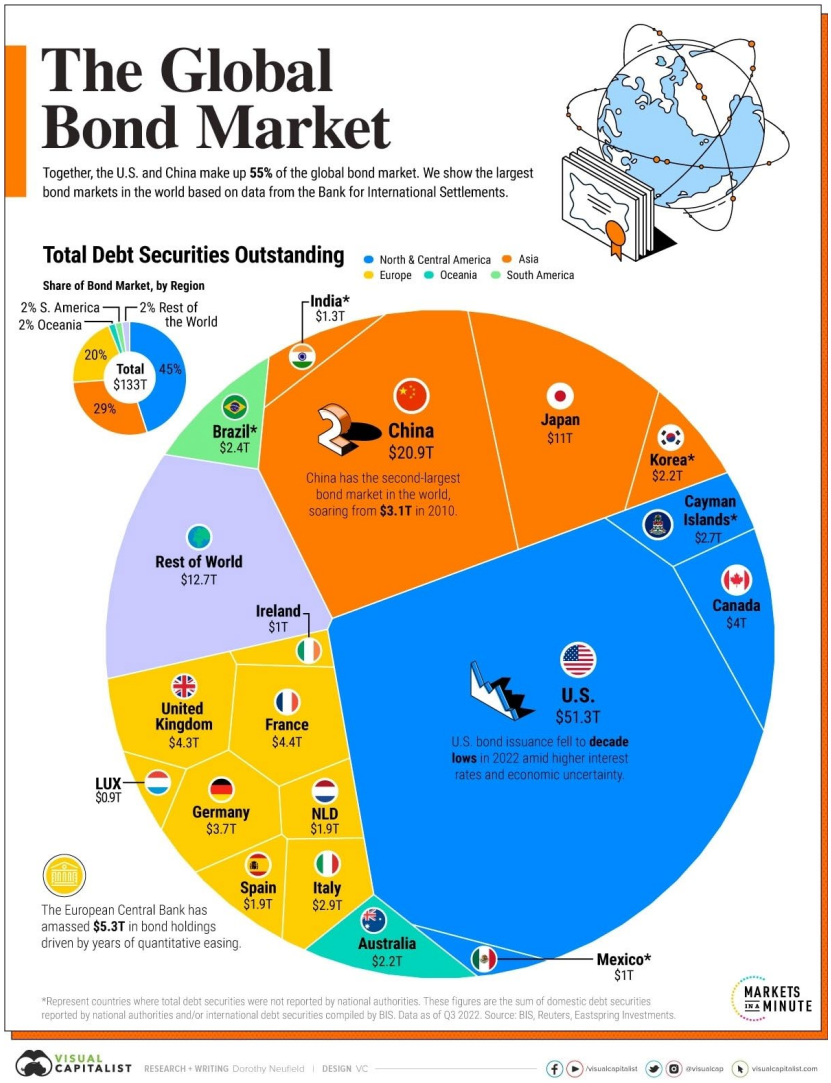
Geographical Distribution and Rankings by Market Capitalization: World

Rank	Country	Market Size (t)	Global Share (%)
1	United States	51.3	39
2	China	20.9	16
3	Japan	11.0	8
4	France	4.4	3
5	United Kingdom	4.3	3
6	Canada	4.0	3
7	Germany	3.7	3
8	Italy	2.9	2
9	Cayman Islands	2.7	2
10	Brazil	2.4	2

Collectively, the bond markets of the United States, China, the European Union, and Japan constitute over 80% of the total global fixed income securities outstanding. SIFMA

The United States maintains the largest bond market globally, with a significant portion comprising government bonds. China's bond market has experienced rapid growth, averaging a 13% annual increase over recent years. World

These figures highlight the concentration of the global bond market within a few major economies, with the U.S. leading by a substantial margin.


The Global Bond Market
Together, the U.S. and China make up 55% of the global bond market. We show the largest bond markets in the world based on data from the Bank for International Settlements.
Total Debt Securities Outstanding
North & Central America
Asia
Europe
Oceania
South America
Share of Bond Market, by Region
2% S. America
2% Oceania
2% Rest of the World
20%
Total $133T
45%
29%
India* $1.3T
Brazil* $2.4T
China $20.9T
China has the second-largest bond market in the world, soaring from $3.1T in 2010.
Japan $11T
Korea* $2.2T
Cayman Islands* $2.7T
Canada $4T
Rest of World $12.7T
Ireland $1T
U.S. $51.3T
U.S. bond issuance fell to decade lows in 2022 amid higher interest rates and economic uncertainty.
United Kingdom $4.3T
France $4.4T
LUX $0.9T
Germany $3.7T
NLD $1.9T
Spain $1.9T
Italy $2.9T
Australia $2.2T
Mexico* $1T
The European Central Bank has amassed $5.3T in bond holdings driven by years of quantitative easing.
*Represent countries where total debt securities were not reported by national authorities. These figures are the sum of domestic debt securities reported by national authorities and/or international debt securities compiled by BIS. Data as of Q3 2022. Source: BIS, Reuters, Eastspring Investments.
MARKETS IN A MINUTE
VISUAL CAPITALIST
RESEARCH + WRITING Dorothy Neufeld
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3-23 Evaluation

Evaluation of the bond market tailored for a private investor across four critical dimensions Liquidity, Risk, Performance, and Costs:

1. Liquidity

Rating: ★★★★☆ (Good but varies)

- Government Bonds (e.g., U.S. Treasuries, German Bunds): Highly liquid, easy to buy and sell with tight bid-ask spreads.
- Corporate Bonds: Vary by issuer and rating. Investment-grade bonds are more liquid than high-yield (junk) bonds.
- Municipal and Emerging Market Bonds: Often less liquid, especially for retail investors.

Key Note**:** Liquidity can dry up during financial stress or for niche, small-issue bonds.

2. Risk

Rating: ★★☆☆☆ to ★★★★☆ (Low to Moderate-High, depending on type)

- Credit Risk: Risk of issuer default (higher in junk bonds, low in sovereign AAA-rated bonds).
- Interest Rate Risk: Bond prices fall when interest rates rise. Long-term bonds are more sensitive.
- Inflation Risk: Fixed income may lose value in real terms if inflation is high.
- Currency Risk: If investing in foreign bonds, FX fluctuations can impact returns.

Safer Options: Short-term government or high-rated corporate bonds.

Riskier: Long-term, high-yield corporate, or emerging market bonds.

3. Performance

Rating: ★★★☆☆ (Stable but modest)

- Average Returns:
    - U.S. Treasuries: ~2–4% annually (historical average).
    - Investment-grade corporates: ~3–5%.
    - High-yield bonds: ~6–9%, but with higher risk.
- Lower volatility than equities—bonds are often used to preserve capital and generate income.
- Returns can be negative in rising interest rate environments.

Bonds don’t usually outperform equities long term, but provide stability and diversification.

4. Costs (Entry/Exit)

Rating: ★★★★☆ (Generally Low for Government Bonds)

- Government Bonds:
  - Low costs if bought directly (e.g., U.S. TreasuryDirect).
  - Narrow spreads and no commissions in many cases.
- Corporate Bonds:
  - Higher spreads, especially for smaller investors.
  - May involve brokerage fees or markups.
- Funds (ETFs, Mutual Funds):
  - Easy access to diversified bond portfolios.
  - Low management fees for passive ETFs (~0.05%–0.50%).

Tax Considerations:

- Interest income is usually taxed as ordinary income.
- Municipal bonds can be tax-free federally (and sometimes at state/local level in the U.S.).

Summary for a Private Investor

Factor	Evaluation
Liquidity	★★★★☆ Strong for gov't bonds, varies elsewhere
Risk	★★★☆☆ Lower than stocks, varies by bond type
Performance	★★★☆☆ Stable income, modest returns
Costs	★★★★☆ Low for gov't bonds, higher for corporates

Tip:

For most private investors, bond ETFs or mutual funds are the easiest and most cost-effective way to gain exposure, diversify risk, and access liquidity.

3-3 Real Estate

3-31 Definition

The real estate market is the sector of the economy that involves the buying, selling, renting, and development of land and buildings. It includes both residential and commercial properties and reflects how property values fluctuate based on supply, demand, interest rates, and economic conditions.

Key Segments of the Real Estate Market

1. **Residential Real Estate**
    - Homes, apartments, condos
    - Owner-occupied or rented
2. **Commercial Real Estate (CRE)**
    - Offices, retail, hotels, industrial properties
    - Typically leased to businesses
3. **Industrial Real Estate**
    - Warehouses, factories, logistics hubs
4. **Land**
    - Undeveloped property, farmland, or land for future development
5. **REITs (Real Estate Investment Trusts)**
    - Companies that own or finance income-producing real estate
    - Traded like stocks; accessible for individual investors

In Simple Terms:

The real estate market is where people and institutions buy, sell, rent, and invest in property—whether it's a family home, a shopping mall, or farmland.

3-32 Size

As of 2025, the global real estate market is projected to reach a total value of approximately $654.39 trillion. Statista

Geographical Distribution and Rankings by Market Capitalization:

1. **Asia-Pacific (APAC):**
    - Market Size: Approximately $328 trillion.
    - Global Share: About 50%.
2. **Europe, Middle East, and Africa (EMEA):**
    - Market Size: Around $196 trillion.
    - Global Share: Approximately 30%.
3. **Americas:**
    - Market Size: Roughly $130 trillion.
    - Global Share: About 20%. MSCI

Segment Distribution:

- **Residential Real Estate:**

- Market Size: Projected to be $534.37 trillion by 2025. Statista
- Global Share: Approximately 81.7% of the total real estate market.

- **Commercial Real Estate:**
  - Market Size: Expected to reach $120.02 trillion by 2025. Statista
  - Global Share**:** About 18.3% of the total real estate market.

These figures underscore the substantial concentration of real estate value in the Asia-Pacific region, particularly within the residential sector. The residential segment overwhelmingly dominates the global real estate market, accounting for over 80% of its total value.

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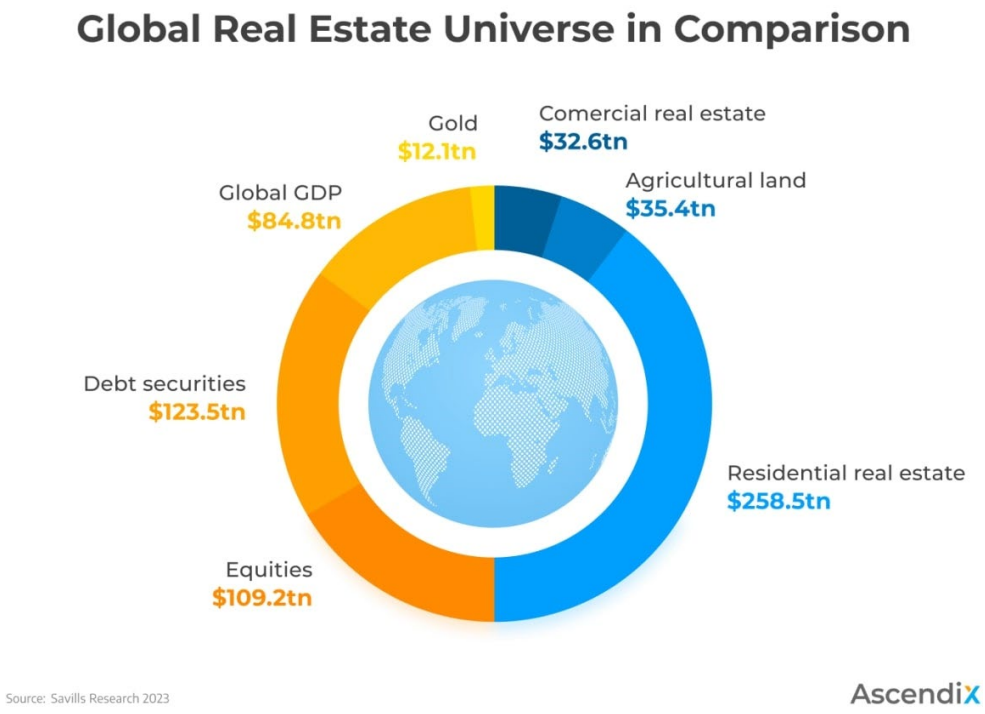
Visual representation of the global real estate market distribution:



3-33 Evaluation

Evaluation of the real estate market for a private investor, covering the four key areas that matter when considering property as an investment class:

1. Liquidity

Rating: ★★☆☆☆ (Low)

- Explanation: Real estate is one of the least liquid asset classes.
    - Selling property can take weeks to months.
    - Market conditions, property type, and location heavily influence how quickly and at what price you can sell.
- Alternative: Investing via REITs (Real Estate Investment Trusts) offers stock-like liquidity.

Bottom Line: Be prepared to lock up capital for years in traditional property investment.

2. Risk

Rating: ★★★☆☆ (Moderate)

- Market Risk: Property values fluctuate with local and global economic conditions, interest rates, and demographic trends.
- Tenant Risk: Rental income can be unstable due to vacancies or non-paying tenants.
- Leverage Risk: Mortgaged properties add financial risk if market prices fall or interest rates rise.
- Natural Disasters & Regulatory Risk: Property may be affected by zoning laws, tax changes, or extreme weather.

Mitigation: Diversify locations, use conservative leverage, and maintain adequate insurance coverage.

3. Performance

Rating: ★★★★☆ (Good long-term)

- Appreciation: Real estate has historically appreciated at 3–5% annually in many developed markets.
- Rental Income: Can provide stable cash flow and act as a hedge against inflation.

- Tax Benefits: Depreciation, mortgage interest deductions, and 1031 exchanges (U.S.) can enhance after-tax returns.
- Leverage: Allows control of a large asset with a relatively small equity investment, boosting returns (and risk).

Note: Performance varies widely by region, property type, and timing.

4. Costs (Entry/Exit)

Rating: ★★☆☆☆ (High)

- Entry Costs:
  - Down payment (10%–30%)
  - Closing costs (2%–5%)
  - Legal and inspection fees
  - Renovation costs (if applicable)
- Ongoing Costs:
  - Property taxes, insurance, maintenance, property management, HOA fees (if applicable)
- Exit Costs:
  - Real estate agent commissions (up to 6% in many countries)
  - Capital gains tax (unless exemptions apply)

REITs and real estate funds offer much lower cost entry/exit points than direct ownership.

Summary for a Private Investor

Factor	Evaluation
Liquidity	★★☆☆☆ Illiquid in traditional form
Risk	★★★☆☆ Moderate, location & leverage sensitive
Performance	★★★★☆ Strong long-term income + appreciation
Costs	★★☆☆☆ High transaction & maintenance costs

Final Tip:

If you're looking for passive income and long-term growth, real estate is a strong contender—but only if you can commit capital for the long haul and handle the operational complexity or outsource it effectively.

3-4 Commodities

3-41 Definition

The commodities market is a global marketplace where raw materials and primary products are bought, sold, or traded, either physically or through derivatives such as futures and options.

Types of Commodities

1. **Hard Commodities** (extracted/mined):
    - Energy: Oil, natural gas, coal
    - Metals: Gold, silver, copper, platinum
2. **Soft Commodities** (grown/harvested):
    - Agricultural: Wheat, corn, coffee, cocoa, cotton, sugar
    - Livestock: Cattle, hogs

Trading Methods

- Spot Market: Immediate delivery of the physical commodity
- Futures Market: Contracts to buy/sell at a future date and price
- Options & Derivatives: Financial instruments based on commodity prices
- ETFs & Indexes: Used by investors to gain exposure without handling physical goods

In Simple Terms:
The commodities market is where people and institutions trade in basic goods like oil, gold, and wheat—things the world needs every day.

3-42 Size

As of 2025, the global commodities market is projected to reach a nominal value of approximately $142.85 trillion. Statista

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3-43 Evaluation

Evaluation of the commodities market from the perspective of a private investor, focusing on the four major investment dimensions:

1. Liquidity

Rating: ★★★★☆ (Good, especially via derivatives and ETFs)

- Highly Liquid Commodities: Crude oil, gold, silver, natural gas—traded heavily on exchanges like NYMEX, COMEX, and ICE.
- Less Liquid: Niche agricultural or industrial commodities (e.g., cocoa, tin, cotton).
- Futures & ETFs: Offer easier access and liquidity without physical delivery hassles.

Bottom Line: Liquidity is generally strong, but varies by commodity and investment vehicle.

2. Risk

Rating: ★★★★☆ (High and volatile)

- Price Volatility: Influenced by geopolitics, weather, supply chain issues, and speculative trading.
    - Example: Oil prices in 2020 went negative due to oversupply and storage shortages.
- Leverage Risk: Commodity futures often involve leverage, which can magnify both gains and losses.
- Event Risk: Sudden shocks (e.g., droughts, wars, OPEC decisions) can cause huge swings.

Mitigation: Use diversified commodity ETFs or indices to spread risk.

3. Performance

Rating: ★★★☆☆ (Variable, cyclical)

- Cyclical Behavior: Commodities move in boom-bust cycles, often inverse to stocks and bonds.

- Inflation Hedge: Commodities (especially gold and energy) perform well during inflationary periods.
- No Yield: Unlike stocks or real estate, commodities don’t generate income—returns rely solely on price changes.

Strategic Use: Commodities are great for portfolio diversification, not necessarily as core long-term holdings.

4. Costs (Entry/Exit)

Rating: ★★★☆☆ (Moderate to High, depending on method)

- Futures Contracts:
  - Low trading fees but require margin accounts, and carry rollover and contango risks.
- ETFs:
  - Low-cost access, but may have management fees and tracking errors.
- Physical Commodities (e.g., gold bullion):
  - Include storage, insurance, and dealer spreads.

Best Access for Private Investors: Commodity ETFs or mutual funds—low barriers and easier management.

Summary for a Private Investor

Factor	Evaluation
Liquidity	★★★★☆ Strong for most widely traded assets
Risk	★★★★☆ High volatility, external event-driven
Performance	★★★☆☆ Inconsistent, good during inflation
Costs	★★★☆☆ Varies by vehicle (futures, ETFs, physical)

Final Tip:
If you're a retail investor, commodities are best used as a tactical allocation (5–15% of your portfolio) for diversification or hedging against inflation and uncertainty.

3-44 Gold

3-441 Definition

The gold market is the global marketplace where gold is traded in various forms—physical, financial, and derivative-based. It includes buying, selling, and investing in gold as a commodity, a store of value, and a financial asset.

How Gold is Traded

1. **Physical Gold:**
    - Bullion (bars and coins)
    - Jewelry and artifacts
    - Stored privately or in vaults
2. **Paper Gold / Financial Instruments:**
    - ETFs (e.g., SPDR Gold Shares – GLD)
    - Futures contracts (e.g., COMEX gold futures)
    - Gold mining stocks and mutual funds
    - Digital gold via fintech apps
3. **Central Bank Reserves:**
    - Many central banks hold gold as part of their foreign reserves.

Main Purposes of the Gold Market

- Store of Value: Used historically to preserve wealth during inflation or crises.
- Safe-Haven Asset: Demand surges in times of economic or geopolitical uncertainty.
- Hedge Against Inflation & Currency Devaluation
- Speculation & Trading: Driven by price movements and technical patterns.

In Simple Terms:

The gold market is where people and institutions buy and sell gold—either as a physical asset or through financial instruments—primarily to store value, hedge against risk, or profit from price changes.

3-442 Size

As of March 2025, the global gold market is valued at approximately $20.8 trillion. Voronoi

Geographical Distribution and Rankings by Market Capitalization:
The valuation of the gold market is based on the total above-ground stock of gold, which is estimated to be around 208,874 metric tonnes. This gold is distributed across various sectors and regions:

- Jewelry: Approximately 95,547 metric tonnes (46% of total above-ground gold).
- Private Investment (Bars and Coins): Around 43,044 metric tonnes (21%).
- Official Holdings (Central Banks): About 35,715 metric tonnes (17%).
- Other Uses (Including ETFs and Industrial Applications): Approximately 34,568 metric tonnes (16%). Companies Sprott Wikipedia

Gold Reserves by Country: Gold's share of forex reserves (February 2025) Wikipedia

Rank	Country	Gold Holdings in t	Share
1	United States	8,133.5	74.9
2	Germany	3,351.5	74.4
3	Italy	2,451.8	70.8
4	France	2,437.0	72.2
5	Russia	2,332.7	29.5
6	China	2,279.6	5.5
7	Switzerland	1,039.9	9.6
8	India	876.1	11.3
9	Japan	845.9	5.7
10	Turkey	765	41.4

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3-443 Evaluation

Evaluation of the gold market specifically for a private investor, examining the key dimensions of investment:

1. Liquidity

Rating: ★★★★☆ (Very High)

- Physical Gold: Moderately liquid—can be sold to dealers, but price negotiation and verification take time.
- Gold ETFs & Futures: Highly liquid—traded on major exchanges (e.g., GLD, COMEX) with tight spreads and high volume.
- Gold Mining Stocks: Liquid like any equity, but performance doesn't always mirror gold prices directly.

Summary: For fast access to cash, gold ETFs and futures are the most liquid; physical gold requires more effort.

2. Risk

Rating: ★★☆☆☆ to ★★★☆☆ (Low to Moderate)

- Price Volatility: Less volatile than stocks, but still subject to swings based on interest rates, inflation, and geopolitical uncertainty.
- No Yield: Gold pays no dividends or interest—it relies solely on capital appreciation.
- Safe-Haven Asset: Often increases in value during crises, inflation, or currency devaluation.
- Currency Risk: For non-USD investors, dollar fluctuations may affect returns.

Summary: Gold is considered low-risk in turbulent times, but underperforms in stable, high-growth environments.

3. Performance

Rating: ★★★☆☆ (Historically modest but stable)

- Long-Term Return: Gold has averaged ~1–2% real return annually over centuries (adjusted for inflation).
- Best Use: Capital preservation, not aggressive growth.

- Strong Performance During Crises: 2008 crisis, COVID-19, and inflationary periods saw sharp price rises.

Summary: Gold is best used as a portfolio stabilizer and inflation hedge, not a growth engine.

4. Costs (Entry/Exit)

Rating: ★★★☆☆ (Moderate, depends on form)

- Physical Gold:
  - Dealer premiums (3%–10% above spot price)
  - Storage and insurance costs
  - Buy-sell spread can be wide
- Gold ETFs:
  - Low management fees (~0.25–0.40%)
  - No storage hassle, instant liquidity
- Gold Futures:
  - Margin requirements, rollover costs
  - Best suited for experienced traders

Tax Note (U.S.): Gold is taxed as a collectible, with a higher capital gains rate (up to 28%).

Summary for a Private Investor

Factor	Evaluation
Liquidity	★★★★☆ Strong, especially via ETFs
Risk	★★★☆☆ Lower than stocks; safe-haven asset
Performance	★★★☆☆ Stable, not aggressive growth
Costs	★★★☆☆ Moderate; depends on form

Final Tip:

Gold is best suited for investors looking to:

- Diversify their portfolio
- Preserve capital
- Hedge against inflation, currency risk, or geopolitical uncertainty

3-5 FOREX

3-51 Definition

The FOREX market (short for Foreign Exchange Market) is the global decentralized marketplace where currencies are traded. It is the largest and most liquid financial market in the world, with an average daily trading volume exceeding $7.5 trillion as of 2024.

Key Features

- Currencies Traded in Pairs: e.g., EUR/USD, USD/JPY, GBP/CHF
  You are buying one currency and selling another simultaneously.
- 24/5 Trading: Open 24 hours a day, five days a week, covering all time zones from Sydney to New York.
- Decentralized Structure: No central exchange; trading occurs via banks, brokers, institutions, and online platforms.

Main Participants

1. Central Banks & Governments – Manage reserves and monetary policy.
2. Commercial Banks & Financial Institutions – Facilitate large-scale transactions.
3. Corporations – Hedge currency exposure from international operations.
4. Speculators & Retail Traders – Aim to profit from price fluctuations.

In Simple Terms:

The FOREX market is where people and institutions buy and sell currencies—like trading dollars for euros or yen for pounds—based on economic trends, geopolitical events, or profit opportunities.

3-52 Size

As of April 2022, the global foreign exchange (FOREX) market experienced an average daily trading volume of approximately $7.5 trillion, marking a 14% increase from 2019. Bank

Geographical Distribution of FOREX Trading:

FOREX trading is predominantly concentrated in major financial hubs. The distribution of global turnover by country is as follows:

1. United Kingdom: 38.1% of global turnover
2. United States: 19.4%
3. Singapore: 9.4%

4. Hong Kong SAR: 7.1%
5. Japan: 4.4% Bank Wikipedia

These five locations collectively account for approximately 78% of total global FOREX trading.

Most Traded Currencies:
The ranking of currencies by their share in global FOREX transactions is as follows:

1. US Dollar (USD): Involved in 88% of all trades
2. Euro (EUR): 31%
3. Japanese Yen (JPY): 17%
4. Pound Sterling (GBP): 13%
5. Chinese Renminbi (CNY): 7% Bank

The US Dollar remains the dominant currency in the FOREX market, being on one side of 88% of all transactions. Notably, the Chinese Renminbi has increased its market share, becoming the fifth most traded currency, up from eighth place in 2019. Bank

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3-53 Evaluation

Evaluation of the FOREX market tailored for a private investor, based on the core dimensions that impact investment decisions:

1. Liquidity

Rating: ★★★★★ (Extremely High)

- Explanation: The FOREX market is the most liquid market in the world with over $7.5 trillion in daily trading volume.
- Major currency pairs (like EUR/USD, USD/JPY) have tight spreads and instant execution almost 24 hours a day.

- Retail traders can open and close positions quickly without significant price slippage (especially with large, stable pairs).

Bottom Line: Liquidity is unmatched—ideal for active traders.

2. Risk

Rating: ★★★★☆ (High)

- Leverage Risk: Retail brokers often offer high leverage (up to 50:1 or more), which magnifies both gains and losses.
- Volatility: Currencies can swing sharply due to interest rates, central bank policy, geopolitics, or economic news.
- Emotional Risk: The fast-paced nature leads to overtrading and psychological stress for unprepared investors.

Mitigation: Limit leverage, use stop-loss orders, and practice risk management strategies.

3. Performance

Rating: ★★★☆☆ (Highly variable)

- No intrinsic value or yield: Unlike stocks or real estate, currencies don't produce income—returns come from price fluctuations only.
- Short-term trading focus: Most retail profits (if any) are short-term; very few succeed consistently over time.
- Hedge Funds & Institutions: Can profit using advanced strategies, but retail performance is generally mixed.

Best suited for: Traders rather than long-term investors.

4. Costs (Entry/Exit)

Rating: ★★★★☆ (Low)

- Spreads: Major pairs often have low spreads (as low as 0.1–1.0 pips).
- No Commissions: Many brokers offer commission-free trading, but profit from spreads.
- Swap/Overnight Fees: Holding positions overnight may incur small rollover charges or credits.
- Low Entry Barriers: You can start with as little as $100–$500 depending on the broker.

Note: Beware of hidden costs with less regulated or offshore brokers.

Summary for a Private Investor

Factor	Evaluation
Liquidity	★★★★★ Extremely liquid
Risk	★★★★☆ High due to leverage & volatility
Performance	★★★☆☆ Depends heavily on trader skill
Costs	★★★★☆ Generally low, especially on major pairs

Final Tip:
The FOREX market is best for experienced or disciplined traders, not passive investors. If you're interested in it, start with a demo account, study technical and macroeconomic analysis, and treat it like a profession—not a hobby.

3-6 Alternatives

3-61 Hedge Funds

3-611 Definition

The hedge fund market is part of the alternative investment universe, consisting of privately managed pooled funds that employ a wide range of complex strategies to generate returns for their investors—regardless of market conditions.

What Is a Hedge Fund?

A hedge fund is an actively managed investment fund that can invest in almost anything: stocks, bonds, currencies, commodities, derivatives, real estate, and even private companies. They often use:

- Leverage (borrowed money)
- Short selling
- Derivatives (options, futures, swaps)
- Global macro, event-driven, or arbitrage strategies

Who Can Invest?

- Typically accredited investors or institutional clients (pension funds, endowments, family offices)
- High minimum investment requirements (often $100,000 to millions)

As an Alternative Asset Class

- Hedge funds fall under alternative investments, distinct from traditional assets like stocks, bonds, or cash.
- Their goal is often absolute return (positive return regardless of market direction).
- Low correlation with traditional markets makes them valuable for diversification.

In Simple Terms:

The hedge fund market is where wealthy investors and institutions pool money into highly flexible, actively managed funds that use sophisticated strategies to seek high returns, manage risk, or diversify away from traditional investments.

3-612 Size

As of 2024, the global hedge fund industry managed approximately $4.5 trillion in assets under management (AUM). Reuters

Geographical Distribution of Hedge Fund AUM:

- North America: Dominates the industry with around 81% of global AUM, totaling approximately $3.95 trillion.
- Europe: Holds about 15.3% of global AUM, equating to approximately $746.6 billion.
- Asia-Pacific and Other Regions: Collectively account for the remaining 3.7% of global AUM. Hedge

Top Countries by Hedge Fund AUM (Approximate Share of Global Total)

1. United States US – ~70% of global hedge fund AUM
2. United Kingdom GB – ~10%
3. Cayman Islands KY – ~5% (many funds domiciled here for regulatory reasons)
4. Hong Kong / Singapore HK SG – ~5% combined
5. Switzerland / Luxembourg CH LU – ~3%

Top Hedge Fund Firms by AUM (as of mid-2024):

1. Bridgewater Associates (USA): $89.6 billion
2. Man Group (UK): $77.5 billion
3. Elliott Investment Management (USA): $69.7 billion
4. Millennium Management (USA): $67.9 billion
5. Citadel LLC (USA): $63.4 billion

These figures highlight the concentration of hedge fund assets in North America, particularly in the United States, which is home to several of the largest hedge fund firms globally.

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3-613 Evaluation

Investing in hedge funds offers unique opportunities and challenges for private investors. Below is an evaluation focusing on Liquidity, Risk, Performance, and Costs associated with hedge fund investments:

1. Liquidity

Rating: ★★☆☆☆ (Low)

- Explanation: Hedge funds typically enforce lock-up periods during which investors cannot withdraw their capital, ranging from several months to years.
- Redemption Restrictions: After the lock-up period, withdrawals may still be limited to specific windows (e.g., quarterly) and require advance notice.
- Exit Challenges: Exiting a hedge fund can incur significant fees and may take several months, making it less liquid compared to traditional investments. Personal

Consideration: Investors should be prepared for reduced access to their capital and assess their liquidity needs accordingly.

2. Risk

Rating: ★★★★☆ (High)

- Leverage: Many hedge funds use borrowed capital to amplify returns, which also increases potential losses.

- Complex Strategies: Utilization of derivatives, short selling, and other sophisticated tactics can introduce significant risk.
- Manager Risk: Performance heavily depends on the fund manager's skill and decisions.
- Market Impact: Hedge funds may be susceptible to market liquidity risks, especially during financial downturns.

Consideration: Thorough due diligence on the fund's strategy, risk management practices, and the manager's track record is essential.

3. Performance

Rating: ★★★☆☆ (Variable)

- Potential for High Returns: Some hedge funds aim for absolute returns, seeking profits in both rising and falling markets.
- Performance Dispersion: Returns can vary widely between funds; some may outperform the market, while others underperform.
- Historical Context: Post-Global Financial Crisis, many hedge funds have struggled to consistently outperform traditional portfolios. Financial https://tinyurl.com/36v4sjtm

Consideration**:** Past performance is not indicative of future results; diversification and realistic expectations are crucial.

4. Costs (Entry/Exit)

Rating: ★★☆☆☆ (High)

- Management Fees: Typically around 2% of assets under management (AUM) annually.
- Performance Fees: Approximately 20% of profits, aligning the manager's incentives with performance. Investopedia
- Additional Expenses: May include administrative fees, trading costs, and potential redemption fees for early withdrawals.

Consideration: High fees can significantly erode net returns; investors should evaluate whether the potential for higher returns justifies the costs.

Summary for a Private Investor

Factor	Evaluation
Liquidity	★★☆☆☆ Limited access to capital
Risk	★★★★☆ High due to leverage and strategies
Performance	★★★☆☆ Variable; potential for high returns but inconsistent
Costs	★★☆☆☆ High fees and expenses

Final Thoughts:

Hedge funds can offer diversification and the potential for high returns but come with significant risks, liquidity constraints, and high fees. Private investors should:

- Conduct Thorough Due Diligence: Understand the fund's strategy, risk profile, and manager credentials.
- Assess Liquidity Needs: Ensure that the investment aligns with their liquidity requirements and investment horizon.
- Evaluate Cost-Benefit: Determine if the potential returns justify the associated fees and expenses.

3-62 Private Equity

3-621 Definition

The Private Equity Market is a segment of the financial industry where investments are made directly into private companies (i.e., those not listed on public stock exchanges) or where public companies are taken private. It is considered an alternative asset class, meaning it falls outside the traditional categories of stocks, bonds, and cash.

Definition:

Private equity is an alternative investment class that involves investing capital into private companies through various strategies such as buyouts, venture capital, growth capital, and distressed investing, with the goal of enhancing value and eventually exiting the investment at a profit—typically through a sale, merger, or public offering.

Key Characteristics:

- Illiquid: Investments are usually locked up for several years.
- Long-term horizon: Returns are realized over time, often 5–10 years.
- Active management: PE firms often take an active role in guiding business strategy and operations.

- High return potential: Historically, private equity has offered higher returns than public markets, though with higher risk.

3-622 Size

The global private equity (PE) market has experienced notable growth and shifts in recent years. Below is an overview of its size, geographical distribution, and rankings by market capitalization and percentage.

Global Market Size

- Assets Under Management (AUM): As of H1 2023, the global private equity market's AUM was $13.1 trillion.
- Fundraising: In 2023, global private markets fundraising totaled $1,046 billion, marking a 22% decline from the prior year. McKinsey

Geographical Distribution

The distribution of private equity assets (H1 2023) varies across regions:

- **North America**:
  - AUM: $4,942 billion.
  - Fundraising: $681 billion (-22% YoY).
- **Europe**:
  - AUM: $2,664 billion.
  - Fundraising: $243 billion (-3% YoY).
- **Asia**:
  - AUM: $2,724 billion.
  - Fundraising: $79 billion (-48% YoY).
- **Rest of world:**
  - AUM: $634 billion.
  - Fundraising: $$43 billion (-41% YoY) McKinsey

These figures highlight North America's leading position in the private equity market, followed by Asia and Europe.

It's important to note that these distributions are influenced by various factors, including economic conditions, regulatory environments, and investor sentiment in each region.

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3-623 Evaluation

Evaluation of the Private Equity (PE) market from the perspective of a private investor, covering the key investment criteria:

1. Liquidity

- Very low liquidity.
- Capital is typically locked for 8–12 years in closed-end PE funds.
- No public market for shares in PE funds; secondary sales are difficult, often at a discount.
- Interim distributions may occur, but full exit happens only at fund maturity or upon asset sale.

Best suited for long-term investors who can afford to part with capital for a decade or more.

2. Risk

- Moderate to high risk, depending on strategy:
    - Buyouts: Moderate risk; target established companies with cash flow.
    - Venture/Growth Capital: Higher risk; target earlier-stage companies.
    - Distressed/Turnaround: High risk, but potentially high reward.
- Risks include:
    - Market cycles (illiquid assets can’t be sold quickly in downturns)
    - Company-level issues (management failure, industry decline)
    - Leverage risk in buyouts (heavily debt-financed deals)

Risk can be mitigated through diversified fund exposure and choosing experienced GPs (general partners).

3. Performance

- Historically strong returns, especially in top-tier funds.
    - Top-quartile PE funds often generate 15–20% IRR (internal rate of return).
    - Outperform public equities over long periods, though with greater dispersion.
- Returns are skewed: a few deals may generate the bulk of profits.
- Performance varies significantly by vintage year and fund manager.

Top-performing PE funds often outperform public markets, but access is key.

4. Costs to Enter and Exit

Entry Costs:

- High barriers to entry:
    - Minimum investments: Typically $250,000 to $5 million.
    - Accredited/institutional investor status usually required.
    - Private placement — no public offering, limited transparency at entry.

Fees:

- "2 and 20" model standard:
    - 2% management fee annually (on committed capital)
    - 20% performance fee (carried interest) above a hurdle rate (~8%)
- Some funds also charge organizational expenses and monitoring fees.

Exit Costs:

- No direct “exit” costs, but:
    - Liquidity comes from fund distribution over time.
    - Selling stakes in the secondary PE market can incur discounts and legal/transaction fees.

High net worth and institutional investors generally benefit more from economies of scale.

Summary Table:

Factor	Evaluation
Liquidity	Very Low — long lock-ups, no active market
Risk	Moderate to High — strategy and manager dependent
Performance	Strong — potential to outperform public markets
Entry Costs	High — large capital requirement, due diligence needed
Exit Costs	Indirect — depends on fund lifecycle or secondary sales

3-63 Venture Capital

3-631 Definition

The venture capital (VC) market as an alternative asset class refers to a segment of private equity investing where capital is provided to early-stage, high-potential startups and emerging companies that are not listed on public exchanges. As an alternative asset class, venture capital stands apart from traditional investments like stocks, bonds, and cash, offering investors exposure to innovation-driven businesses with the potential for outsized returns—but also with higher risk, longer time horizons, and lower liquidity.

Venture capital typically involves staged financing by specialized VC firms or funds in exchange for equity, and it plays a critical role in fostering entrepreneurship, technological advancement, and economic growth.

Key Characteristics of Venture Capital

1. **Stage of Investment**
    - Focuses on early-stage, high-growth potential startups.
    - Includes seed, Series A/B/C funding rounds, and sometimes growth equity.
2. **Risk Profile**
    - High risk due to business model uncertainty, market competition, and lack of operating history.
    - Many startups fail, but a few “home runs” can deliver outsized returns.
3. **Return Potential**
    - Very high potential returns, especially if invested early in successful companies (e.g., early investors in Uber, Airbnb).
    - Returns are skewed—majority of gains often come from a small number of portfolio companies.
4. **Liquidity**
    - Low liquidity: investments are locked up for years (usually 7–10 years).
    - No public market; exits occur via IPOs, acquisitions, or secondary sales.
5. **Time Horizon**
    - Long-term investment required to realize gains.
    - Illiquid until exit event.
6. **Access**
    - Typically limited to institutional investors, family offices, and qualified high-net-worth individuals due to regulatory and capital requirements.

7. **Active Involvement**
    - VC firms often take an active role in management: board seats, strategic guidance, hiring support.
8. **Valuation**
    - Based on private negotiations rather than market pricing.
    - Difficult to benchmark consistently.

3-632 Size

In 2024, global venture capital (VC) investments totaled approximately $368.3 billion, marking a 5.4% increase from $349.4 billion in 2023. KPMG

Geographical Distribution of VC Investments in 2024

- **Americas**: Led with $221.7 billion in VC investments, with the United States accounting for $209 billion of this total.
- **Asia-Pacific**: Experienced a decline, with VC investments dropping to $78.8 billion, the lowest in nine years.
- **Europe**: Saw a slight decrease in VC investments, totaling $62.4 billion, down from $67.6 billion in 2023. KPMG

Rankings by Market Capitalization and Percentage

While specific rankings by market capitalization and percentage are not detailed in the provided sources, the United States maintained a dominant position, capturing a significant portion of global VC investments. Europe and the Asia-Pacific regions followed, with notable variations in investment levels across different countries within these regions.

It's also noteworthy that in 2024, artificial intelligence (AI) companies attracted substantial VC funding, accounting for nearly one-third of all global venture capital investments. Major AI firms like xAI, Databricks, Anthropic, and OpenAI collectively raised approximately $40 billion. Allvue Systems Barron's

These figures underscore the dynamic nature of the global venture capital landscape, with significant contributions from various regions and a pronounced emphasis on emerging technologies such as AI.

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3-633 Evaluation

Evaluation of the Venture Capital (VC) market from the perspective of a private investor, covering key criteria: liquidity, risk, performance, and costs to enter and exit.

1. Liquidity:

- Low liquidity.
- VC investments are typically locked in for 7–10 years.
- No secondary market for most positions; exits usually depend on IPOs, acquisitions, or secondary sales.
- Interim liquidity is rare, making it unsuitable for investors needing short-term access to capital.

2. Risk:

- High risk.
- Startups (main VC targets) have a high failure rate.
- Returns are skewed — a small percentage of investments produce most gains.
- Risks include:
    - Market volatility
    - Regulatory changes
    - Technology disruption
    - Execution failure by founders

3. Performance:

- Potential for high returns, but highly variable.
- Top-tier VC funds (e.g., Sequoia, Andreessen Horowitz) have delivered annualized returns of 20–30%.
- Average VC returns are closer to 10–15% IRR over a fund's life.

- Strong returns are often concentrated in a few unicorns (e.g., early investments in Airbnb, Uber, etc.).

4. Costs to Enter and Exit:

Entry Costs:

- High minimum investment: Typically $250,000–$1 million+ for direct fund participation.
- Indirect access (via feeder funds or VC ETFs) has lower minimums but often higher fees.
- Investors must qualify as accredited (in most jurisdictions).

Exit Costs:

- Not standardized, as exits depend on portfolio companies' IPOs or acquisitions.
- Carry (carried interest): Fund managers often take 20% of profits above a set hurdle rate (typically ~8%).
- Management fees: Usually 2% annually of committed capital, regardless of performance.
- Secondary market sales, if allowed, may involve steep discounts and legal fees.

Summary Table:

Factor	Evaluation
Liquidity	Low — capital locked for years
Risk	High — startup failure rate, illiquidity
Performance	High potential — but dependent on manager/fund
Entry Costs	High — large minimums and accreditation needed
Exit Costs	Moderate — carried interest, long wait for liquidity

Comparison with Traditional Asset Classes

Feature	Venture Capital	Stocks	Bonds	Real Estate
Liquidity	Very Low	High	Moderate to High	Low to Moderate
Risk Level	Very High	Moderate to High	Low to Moderate	Moderate
Return Potential	Very High (if successful)	Moderate to High	Low to Moderate	Moderate to High
Time Horizon	Long (7–10+ years)	Short to Long	Short to Long	Medium to Long
Volatility	Low (valuation intervals)	High (market-driven)	Low	Low to Moderate

Access	Limited (accredited)	Broad (public markets)	Broad	Moderate
Income Yield	None (until exit)	Dividends (some)	Regular interest	Rental income (if any)
Diversification	Requires fund strategy	Easy through ETFs/indexes	Easy	Requires capital & time

3-7 Collectibles

3-71 Definition

The collectibles market is an alternative asset class that involves investing in unique, tangible items that are valued for their rarity, cultural significance, aesthetic appeal, or historical importance—rather than traditional financial metrics like cash flow or dividends.

These items can include:

- Art (paintings, sculptures)
- Wines & spirits
- Classic cars
- Rare coins & stamps
- Luxury watches
- Sports memorabilia
- Vintage comics, toys, and trading cards
- NFTs and digital collectibles

Key Characteristics:

- Tangible & unique: Each item is non-fungible, often one-of-a-kind or limited-edition.
- Illiquid: Difficult to sell quickly; transactions are often private or through auctions.
- Value appreciation: Driven by scarcity, condition, provenance, and collector demand.
- Uncorrelated returns: Prices often move independently of stock and bond markets.
- Passion-driven: Many investors are also enthusiasts or collectors.

Summary:

Collectibles as an asset class offer diversification and inflation hedging potential, but they come with challenges like valuation uncertainty, storage/security needs, and liquidity constraints.

Comparison

Category	Collectibles	Private Equity	Venture Capital	Real Estate	Hedge Funds
Asset Type	Tangible, unique items (e.g., art, wine, cars)	Private company equity (usually mature)	Early-stage private company equity	Physical or income-producing property	Pooled funds using complex trading strategies
Liquidity	Very low — resale often slow, depends on demand	Low — capital tied up 8–12 years	Low — long lock-up, typically 7–10 years	Moderate — can sell property but takes time	Moderate — can have redemption restrictions
Valuation	Subjective — depends on market sentiment, rarity	Market-based but complex	Highly speculative and variable	Market comps, appraisals	NAV or fund valuation metrics
Volatility	High — prices can swing based on trends or hype	Moderate — long-term returns but risky	High — high failure rate for startups	Low to moderate — depends on market cycles	Varies — depends on strategy
Return Potential	High — unique pieces can appreciate significantly	High — top funds deliver strong IRRs	Very high — unicorn potential	Steady — income + appreciation	Moderate to high — strategy-driven
Diversification	Strong — low correlation to financial markets	Strong — low correlation	Strong — though tied to tech cycles	Good — tangible and defensive in inflation	Strong — often designed to hedge
Access	Moderate — auctions, dealers, platforms	Limited — high minimums, accredited investors only	Limited — high minimums, GP/LP structure	Moderate — REITs for liquid access	Often exclusive — high net worth or institutional
Costs	High — storage, insurance, auction fees	High — management + carried interest	High — same as PE + higher risk	Moderate — taxes, upkeep, broker fees	High — 2 and 20 model still common

Summary Insights

- Collectibles: Best for passionate investors looking for non-financial returns and long-term appreciation, but requires deep knowledge and tolerance for illiquidity.
- Private Equity & VC: Strong return potential but require large capital and long commitment periods.

- Real Estate: Income-producing and tangible; more accessible via REITs.
- Hedge Funds: Flexible and diverse strategies; often less accessible and fee-heavy.

3-72 Size

The global collectibles market has shown significant growth, with varying estimates reflecting its expansive and diverse nature.

Market Size Estimates

- Grand View Research (2023): Estimated the market at $294.23 billion in 2023, projecting growth to $422.56 billion by 2030, with a compound annual growth rate (CAGR) of 5.5% from 2024 to 2030. Grand
- Market Decipher (2024): Reported an estimated market size of $496.2 billion in 2025, with a Compound Annual Growth Rate of 7.4%. https://tinyurl.com/3592jkyc

These discrepancies highlight the challenges in quantifying the market, likely due to differences in definitions, segments included, and valuation methodologies.

Geographical Distribution

- Europe: Dominated the market with a 36.89% share in 2023, attributed to its rich cultural heritage and strong traditions in art and antique collecting.
- North America: Held a 24.45% share in 2023, driven by a robust economy and high disposable incomes, enabling investments in high-value collectibles.
- Asia-Pacific: Projected to experience the fastest growth, with a CAGR of 6.4% from 2024 to 2030, fueled by rapid economic development and increasing disposable incomes in countries like China and India. Grand

Market Dynamics

- Art & Antiques: Led the market with a 33.65% revenue share in 2023, reflecting a growing appreciation for unique items with historical significance.
- Toys & Action Figures: Anticipated to grow at the fastest CAGR of 7.0% from 2024 to 2030, driven by nostalgia and the influence of pop culture. Grand

The market is also witnessing a surge in interest from younger demographics, particularly in the Asia-Pacific region, where millennials and Gen Z are increasingly participating in collectibles, especially in sectors like art and luxury items. Reuters

In summary, while estimates of the global collectibles market size vary, it is evident that the market is substantial and poised for continued growth, with Europe currently leading in market share and the Asia-Pacific region emerging as a rapidly expanding market.

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3-73 Evaluation

Evaluation of the Collectibles Market for a private investor, based on key investment factors: Liquidity, Risk, Performance, and Costs to Enter and Exit.

1. Liquidity

- Very low liquidity.
- Collectibles often take weeks or months to sell, typically through auctions, dealers, or private sales.
- No centralized or standardized market like stocks or real estate.
- Market demand fluctuates, and selling quickly may require accepting a lower price.

More liquid items include high-end watches or art by well-known artists, which have active auction markets.

2. Risk

- Moderate to high risk, depending on the category:
  - Art, wine, vintage cars: Often stable if well-researched.
  - Niche or pop culture items: Prone to hype cycles and sudden crashes.
- Market is sentiment-driven — values influenced by trends, pop culture, generational interest.
- Authenticity, condition, and provenance are major risks — fakes or poor condition drastically reduce value.
- Lack of price transparency can hinder valuation.

Experienced collectors who understand the market tend to manage risk better.

3. Performance

- Potential for high long-term returns, especially for rare, in-demand items:
    - Art: Long-term average ~5–7% CAGR (top artists exceed this)
    - Wine: 8–10% CAGR for top vintages (Liv-ex indices)
    - Watches: Some Rolex and Patek Philippe models have outpaced equities
- Returns are not consistent and often rely on unique item appreciation.
- Low correlation with financial markets — useful as a diversification tool.

Collectibles can act as a hedge against inflation or market downturns.

4. Costs to Enter and Exit

Entry Costs:

- Variable, often high:
    - Art: Entry points range from $5,000 to millions
    - Wine: Starting at $1,000 for investment-grade cases
    - Watches: High-end pieces start around $10,000+
- Fees: Buyer's premium (auction), dealer margins, import taxes, VAT.

Holding Costs:

- Significant for physical items:
    - Insurance
    - Storage (climate-controlled for art, wine)
    - Maintenance (restoration, conservation)

Exit Costs:

- Seller’s fees: Auction houses charge 10–25% commission.
- May face capital gains taxes depending on jurisdiction.
- Time to sell can be lengthy and unpredictable.

Fractional ownership platforms and marketplaces (e.g., Masterworks, Rally, Vinovest) lower entry thresholds, but come with platform fees.

Summary Table:

Factor	Evaluation
Liquidity	Very Low — difficult and slow to sell
Risk	Moderate to High — value tied to trends and condition
Performance	High potential — especially with top-tier assets

Entry Costs	Medium to High — item-dependent, plus insurance/storage
Exit Costs	Moderate — auction fees, long sale cycles, taxes

Top Collectible Categories for Investors

Category	Highlights
Fine Art	Blue-chip artists (e.g., Warhol, Basquiat, Picasso); long-term appreciation
Luxury Watches	Rolex, Patek Philippe, Audemars Piguet; limited editions drive demand
Wine & Whiskey	Bordeaux, Burgundy, Scotch; ages well, tradable via indices (e.g., Liv-ex)
Classic Cars	Ferrari, Porsche, Aston Martin; highly illiquid but very high upside
Rare Coins	Historical and limited mintage coins; well-established market
Sports Memorabilia	Game-worn gear, rookie cards (Jordan, Mantle); rising in value
Vintage Comics	Marvel/DC first editions; nostalgic demand with Gen X and Millennials
Trading Cards	Pokémon, Magic: The Gathering, rare sports cards; high speculative value
NFTs & Digital Collectibles	Speculative and volatile, but some blue-chip NFTs retain value

Top Platforms for Private Investors

Platform	Focus Category	Features
Masterworks	Fine Art	Fractional shares of blue-chip art; SEC-registered; low minimums
Rally	Multicategory (cars, cards, comics, etc.)	Buy/sell fractional shares of collectibles via mobile app
Collectable	Sports Memorabilia	Offers SEC-qualified offerings in iconic sports items
Vinovest	Fine Wine	Managed wine investment portfolios; insured storage
MyRacehorse	Racehorses	Micro-shares in thoroughbred horses with real-time performance tracking
Alt.xyz	Trading Cards & Sports	Buy/sell and track values of cards with analytics and portfolio tools
Fractional.art	Digital Collectibles (NFTs)	Invest in fractions of top-tier NFTs like CryptoPunks, Fidenzas
PWCC & Goldin Auctions	Auctions (Cards, Memorabilia)	Buy rare cards and collectibles at auction

Sotheby's & Christie's	Fine Art & Luxury	Traditional auction houses; high-end items with global visibility

Notes for Investors:

- Start with what you understand or love — passion often drives better outcomes in collectibles.
- Do your homework: Authentication, provenance, market comps, and insurance are key.
- Use platforms that offer transparency, SEC compliance, and secondary market access if possible.

Collectibles Investment Checklist

1. Authenticity

- Verified by recognized authority or third-party authentication service
- Includes certificate of authenticity (COA), expert appraisal, or provenance
- Cross-checked against known forgeries, databases, or serial numbers

2. Provenance (Ownership History)

- Clear record of previous ownership (especially important for art, antiques, luxury items)
- No legal disputes or stolen property claims
- Relevant exhibition, auction, or sales history

3. Condition & Preservation

- Item is in excellent or investment-grade condition (graded if applicable)
- Professionally stored or properly maintained
- No hidden damage or deterioration (e.g., fading, mold, scratches, tears)

4. Market Demand

- Item/category has a strong and active collector base
- Historical appreciation trends are positive (e.g., tracked via auction results, indexes)
- Comparable items have recently sold with price stability or growth

5. Rarity & Scarcity

- Limited edition or low production numbers
- Includes unique attributes (e.g., first editions, artist-signed, one-of-a-kind)
- Rarity documented or listed by reputable sources

6. Valuation

- Independently appraised by a qualified professional
- Comparable sales data from recent auctions or marketplaces
- Price aligns with current market trends — not overhyped

7. Liquidity & Exit Potential

- Can be sold through recognized platforms or auction houses
- Resale market exists and is relatively active
- Understand holding period and potential time-to-sell

8. Costs

- Considered entry cost + fees (buyer's premium, shipping, tax)
- Factored in storage, insurance, and maintenance costs
- Resale costs understood (e.g., auction house seller fees up to 25%)

9. Legal & Regulatory

- Complies with import/export laws if applicable
- Ownership is transferable without legal restrictions
- Tax implications (e.g., capital gains taxes) are understood

10. Personal Interest (Bonus for Passion Investors)

- You genuinely enjoy or understand the category
- Willing to hold long-term even if the item takes time to sell
- Comfortable displaying or storing it (if physical

3-8 Crypto

3-81 Definition

The cryptocurrency market is a digital and decentralized alternative asset class composed of cryptographically secured digital assets—primarily based on blockchain technology—that function as mediums of exchange, stores of value, or platforms for decentralized applications.

Definition:
Cryptocurrencies are digital assets that use blockchain and cryptography to enable peer-to-peer transactions, independent of centralized financial institutions. As an alternative asset

class, they provide non-traditional exposure to innovation, decentralization, and high-growth markets.

Key Characteristics:

- Decentralized: Operates without intermediaries (e.g., banks or governments)
- Digital-native: Exists only in digital form and is transferred electronically
- Highly volatile: Subject to large and rapid price swings
- Transparent: Transactions recorded on public, immutable ledgers (blockchains)
- Programmable: Many tokens (e.g., Ethereum) enable smart contracts and DeFi use cases

Examples:

- Bitcoin (BTC) – Store of value, digital gold
- Ethereum (ETH) – Smart contract and DeFi platform
- Solana, Avalanche, Polygon – Layer 1/2 networks for scalable dApps
- Stablecoins (USDT, USDC) – Pegged to fiat currency, used for trading & settlement

Role in a Portfolio:

- Offers high return potential and diversification due to low correlation with traditional markets
- Acts as a hedge against currency debasement/inflation (especially BTC)
- Considered speculative and high-risk, best suited for small allocation within an alternative assets sleeve

Crypto vs Other Alternative Asset Classes

Category	Cryptocurrency	Private Equity	Venture Capital	Collectibles	Real Estate
Asset Type	Digital tokens on blockchain (e.g., BTC, ETH)	Equity in private companies (usually mature)	Equity in startups and early-stage companies	Tangible rare items (art, wine, cars, etc.)	Tangible property; land or income-producing assets
Liquidity	High — 24/7 trading on exchanges	Very Low — 8–12 year lock-ups	Very Low — long-term lock-up	Very Low — illiquid, auction-based	Moderate — can sell but takes time
Volatility	Extremely High — driven by sentiment/news	Moderate — varies by deal cycle	High — startup failure risk	High — trends and hype-sensitive	Low to Moderate — depends on location

Return Potential	Very High — BTC, ETH have seen massive gains	High — especially in top-tier funds	Very High — unicorn potential	High — rare items can greatly appreciate	Moderate to High — income + capital gains
Transparency	High — blockchain records are public	Low — private data, opaque reporting	Low — depends on fund and startup disclosure	Low — subjective valuation, inconsistent data	Moderate — appraisals and property records
Diversification	Strong — low correlation to stocks/bonds	Strong — not correlated to public markets	Strong — though tied to tech cycles	Strong — driven by cultural trends	Strong — tangible and long-term hedge
Access	Easy — retail-friendly (Coinbase, Binance, etc.)	Hard — accredited investors only	Hard — high minimums, institutional preference	Moderate — growing access via fractional platforms	Moderate — REITs improve accessibility
Fees	Low to Moderate — exchange and blockchain fees	High — 2% management + 20% carried interest	High — similar to PE with higher risk	High — storage, insurance, auction commissions	Moderate — broker fees, taxes, upkeep
Regulation	Evolving — varies by country	Established — strong legal frameworks	Established — VC structures are well-defined	Light — mostly buyer/seller protection	Well-regulated — legal ownership rights enforced

Summary Insights

- Cryptocurrency is best for investors seeking liquidity, high upside, and innovation exposure, but must accept extreme volatility and regulatory uncertainty.
- Private Equity & VC deliver strong long-term returns but require capital lock-up and selective access.
- Collectibles offer diversification and passion-driven appeal, though they are illiquid and hard to value.
- Real Estate is more stable and income-generating, suited for long-term wealth preservation.

3-82 Size

As of early April 2025, the global cryptocurrency market is valued at approximately $2.53 trillion, reflecting a decrease of about 6.85% compared to the previous year. This market

encompasses a diverse range of digital assets, with Bitcoin maintaining a dominant position, accounting for 60.7% of the total market capitalization. Coin

Market Distribution by Region:

- **North America:** Between July 2023 and June 2024, North America received an estimated $1.3 trillion in on-chain cryptocurrency value, representing approximately 22.5% of global activity. This substantial share is largely driven by institutional investments and the introduction of Bitcoin Exchange-Traded Products (ETPs) in the United States. Chainalysis+1
- **Europe:** In 2024, Europe accounted for over 39.5% of the global cryptocurrency market. The implementation of the Markets in Crypto-Assets (MiCA) regulation has fostered a pro-crypto environment across the European Union, attracting significant investor attention and positioning the region as a leader in digital asset regulation. https://tinyurl.com/5h4aj2cx
- **Asia-Pacific:** The Asia-Pacific region has witnessed rapid growth in cryptocurrency adoption, with countries like India and Vietnam leading in terms of the number of cryptocurrency owners. This surge is attributed to the increasing demand for accessible financial solutions and technological innovations in the region. Market

Cryptocurrency Ownership:

As of December 2024, the number of cryptocurrency owners worldwide reached approximately 659 million, marking a 13% increase from January 2024. This growth is driven by factors such as the approval of cryptocurrency ETFs, pro-crypto policies in various countries, and the increasing acceptance of digital assets by institutional investors. Crypto

The global cryptocurrency market continues to evolve, with regional dynamics influenced by regulatory developments, technological advancements, and varying levels of institutional adoption.

Sources Library		
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https://tinyurl.com/5h4aj2cx	https://tinyurl.com/4re7w93h	https://tinyurl.com/yjyun92n
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https://tinyurl.com/3zsb7x4v	https://tinyurl.com/3rvsc9wz	https://tinyurl.com/2s45mhpe
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https://tinyurl.com/4t6pn3yd		

3-83 Evaluation

Evaluation of the cryptocurrency market from the perspective of a private investor, focusing on Liquidity, Risk, Performance, and Entry/Exit Costs:

1. Liquidity

- High for Major Coins: Bitcoin (BTC) and Ethereum (ETH) are highly liquid, with 24/7 trading on global exchanges and significant daily volume (e.g., BTC trades over $20 billion/day).
- Lower for Altcoins: Many smaller coins have lower trading volumes and can suffer from slippage during large trades.
- Availability: Liquidity is accessible across centralized exchanges (e.g., Binance, Coinbase) and decentralized platforms (e.g., Uniswap), though fiat-to-crypto pairs are generally smoother on centralized exchanges.

Investor takeaway: Liquidity is strong in large-cap assets, but be cautious with small-cap tokens where it may be harder to exit without impacting price.

2. Risk

- Volatility: Prices can fluctuate dramatically in short time frames (BTC can move 5–10% in a day).
- Regulatory: Varies by jurisdiction; unclear regulations or outright bans (e.g., China) can affect asset value.
- Custodial Risk: Keeping assets on exchanges can be risky (hacks, bankruptcies), while self-custody (e.g., hardware wallets) requires technical diligence.
- Scams/Fraud: The space still contains a large number of scams and rug-pulls, especially in decentralized finance (DeFi) and meme coins.

Investor takeaway: Crypto carries high systemic and idiosyncratic risk. Allocate capital accordingly, and use trusted platforms or cold storage for safety.

3. Performance

- Long-Term: Bitcoin has returned over 100,000% since inception. The last 10 years have included multiple bull and bear cycles.
- 2023–2024: BTC and ETH outperformed many traditional assets, especially with institutional adoption and Bitcoin ETFs entering the U.S. market.
- Diversification: Correlation with tech stocks (like NASDAQ) increases during risk-on periods, but crypto remains a distinct asset class.

Investor takeaway: While past performance has been stellar, it is not guaranteed, and timing the market is notoriously difficult.

4. Costs to Enter and Exit

- Exchange Fees:
  - Centralized exchanges charge ~0.1%–0.5% per trade.
  - Decentralized exchanges (DEXs) charge variable network fees (e.g., gas on Ethereum).
- Spreads: Varies by asset and exchange; tighter for major tokens, wider for illiquid ones.
- Slippage: Can be significant for large trades in low-volume assets.
- Fiat On-Ramp/Off-Ramp: Credit card/bank transfers may incur 1–3% fees and have regulatory KYC processes.

Investor takeaway: Costs are generally low for top-tier tokens on major platforms, but increase significantly for altcoins and decentralized trades. Fiat on/off ramps can be slower and more expensive.

Summary for a Private Investor

Factor	Rating	Notes
Liquidity	☆☆☆☆☆	Excellent for BTC/ETH, moderate for altcoins
Risk	☆☆☆☆☆	High risk due to volatility, regulation, and scams
Performance	☆☆☆☆☆	Historically strong, but cyclical and speculative
Entry/Exit Costs	☆☆☆☆☆	Reasonable for major coins, higher for altcoins or DeFi

3-9 Comparison

Comparison of major asset classes from the perspective of a private investor, evaluating Liquidity, Risk, Performance, and Entry/Exit Costs:

Asset Class Comparison Table

Asset Class	Liquidity	Risk	Historical Performance	Entry/Exit Costs
Stocks	★★★★☆	★★★☆	7–10% annually (long-term)	Low (0.1–0.5%)
Bonds	★★★★☆	★★☆☆	2–5% annually	Low (bid-ask spread, commissions)
Real Estate	★☆☆☆☆	★★☆	6–9% annually (varies by market)	High (5–10% total: agent, legal, taxes)
Commodities	★★☆☆	★★★☆	Highly cyclical	Medium (futures: moderate, ETFs: low)
FOREX	★★★★★	★★★★	Short-term potential, low long-term	Low (spreads, leverage risks)
Alternatives (HF/PE/VC)	★☆☆☆	★★★★	10–25%+ (but with huge variance)	Very High (2/20 fees, illiquidity)
Collectibles	★☆☆☆	★★★★	Highly variable, subjective	High (auctions, storage, authentication)
Crypto	★★★★☆	★★★★	50–100%+ bull years, -80% bear	Medium (0.1–1% fees + volatility/slippage)

Summary Table (Emoji Legend)

Legend	★★★★★ = Excellent	★ = Poor
Liquidity = How easily you can buy/sell		
Risk = Market volatility and downside		
Performance = Historical returns (adjusted for risk)		
Entry/Exit Costs = Fees, friction, effort to access/liquidate		

Detailed Breakdown by Category

Stocks

- Liquidity: Highly liquid, especially for large-cap public equities.
- Risk: Moderate. Diversifiable with ETFs. Sensitive to economic cycles.

- Performance: Long-term compounding has outpaced inflation.
- Costs: Minimal with online brokers (commission-free trading common).

Bonds

- Liquidity: High for government and investment-grade corporate bonds.
- Risk: Interest rate risk, credit/default risk (lower for gov't).
- Performance: Stable income, but inflation erodes returns.
- Costs: Low, but spreads can be wider in less-traded issues.

Real Estate

- Liquidity: Very low — takes weeks/months to buy or sell.
- Risk: Location-specific; interest rate sensitive.
- Performance: Strong over long periods; includes rental income.
- Costs: High — agent fees, taxes, legal, maintenance, mortgage friction.

Commodities (Gold, Oil, Agri, etc.)

- Liquidity: Decent for major assets (gold, oil); low for others.
- Risk: High — tied to geopolitics, weather, inflation.
- Performance: Cyclical; useful as an inflation hedge.
- Costs: Low via ETFs, moderate with futures (margin, roll yield).

FOREX

- Liquidity: Extremely high — largest financial market globally.
- Risk: High — leverage amplifies losses.
- Performance: Low for long-term investors; better for short-term/speculators.
- Costs: Low spreads, but leverage + volatility can be costly.

Alternatives (Hedge Funds, PE, VC)

- Liquidity: Very low — lock-up periods from years to a decade.
- Risk: Very high, especially VC; less transparent.
- Performance: High upside, but access and selection are critical.
- Costs: Very high — traditional 2/20 fee model and access barriers.

Collectibles (Art, Wine, Watches, etc.)

- Liquidity: Poor — niche buyers and long sales cycles.
- Risk: High — subjective valuations, damage, fraud risk.
- Performance: Can outperform in rare cases; most underperform.
- Costs: High — storage, insurance, authentication, auction fees.

Cryptocurrency

- Liquidity: High for majors (BTC/ETH); variable for altcoins.
- Risk: Extreme volatility, regulatory risk, custody risk.
- Performance: Historically strong; boom-bust cycles.
- Costs: Moderate — exchange fees, spreads, slippage, gas fees (DeFi).

Chapter 4

Rules of Investing

4-1 Golden Rules

Your Golden Rules

1. **Liquidity** – Smart. You never want to be stuck when you need to exit.
2. **Diversification** – Classic for a reason. It protects you from the unknown.
3. **Performance** – Yes, returns matter, but it's good you're not putting it first.
4. **Risk Management** – Arguably the heart of it all. Protecting capital is the game.
5. **Keep it Simple** – Love this. Complexity often hides risk or costs.

What You Might Consider Adding

- **Time Horizon / Patience** – Investments behave differently over short vs. long periods. Knowing your time horizon shapes everything.
- **Cost Awareness** – Fees, taxes, spreads, slippage. They quietly eat returns.
- **Behavioral Discipline** – Even the best strategy fails if emotion overrides logic. Consistency beats brilliance in the long run.
- **Alignment with Goals** – Every investment should map to a purpose (retirement, income, growth, etc.).

4-11 Liquidity

What Does Liquidity Mean?

Liquidity refers to how quickly and easily you can convert an investment into cash without significantly affecting its value.

- High Liquidity = Easy to sell quickly (e.g., cash, stocks on major exchanges)
- Low Liquidity = Difficult to sell quickly or may require a discount (e.g., real estate, collectibles, private equity)

Why Liquidity Is Important

1. **Emergency Access**
   Life throws curveballs—having liquid assets means you can respond without panic selling.
2. **Tactical Flexibility**
   Being liquid gives you freedom to pivot, seize new opportunities, or rebalance your portfolio.
3. **Risk Management**
   Illiquid assets often come with higher risk, including market freezes or forced sales at loss.

4. **Avoids Lock-In Stress**
   When markets turn volatile, illiquid holdings can trap you in bad positions with no easy exit.

How to Achieve Liquidity

1. **Hold a Cash Reserve**
   Always keep a portion of your portfolio in cash or near-cash instruments (e.g., money market funds).
2. **Balance Liquid vs. Illiquid Assets**
   Real estate, private investments, or long-term bonds should be balanced with liquid holdings like stocks, ETFs, and cash.
3. **Understand Lock-Up Periods**
   Know if funds or investments have lock-ins (e.g., hedge funds, retirement accounts, CDs).
4. **Use Liquid Investment Vehicles**
   Favor instruments traded on major exchanges with strong daily volume.
5. **Set Rules for Rebalancing**
   Periodically reassess liquidity across your portfolio and adjust if necessary.

Common Mistakes to Avoid

- Investing too heavily in illiquid assets without adequate cash buffer.
- Ignoring the time it takes to sell certain investments in a down market.
- Chasing high returns in locked-up products without understanding the exit risks.

Rule of Thumb: At least 10-20% of your portfolio should be in highly liquid assets

Liquidity

The ease of converting investments to cash without loss.

WHY IT MATTERS

- Access funds in emergencies
- Stay flexible in market shifts
- Avoid being stuck in bad positions

HOW TO ACHIEVE

- Hold a cash buffer
- Balance liquid vs. illiquid assets
- Use ETFs, stocks, money market funds
- Watch out for lock-up periods

WATCH OUT FOR

- Overloading on illiquid assets
- Ignoring exit timelines
- Misjudging marketability in downturns

RULE OF THUMB: At least 10–20% of your portfolio should be in highly liquid assets.

4-12 Diversification

What Is Diversification?

Diversification is the strategy of spreading your investments across different assets, sectors, or geographies to reduce overall risk. “Don’t put all your eggs in one basket.” It’s not about avoiding risk—it’s about managing it smartly by not relying on the success of a single investment.

Why Diversification Is Important

1. **Risk Reduction**
   Losses in one area can be offset by gains in another, helping smooth returns over time.
2. **Protects Against the Unknown**
   No one can predict which asset or sector will outperform. Diversification builds resilience.
3. **Improves Risk-Adjusted Returns**
   A well-diversified portfolio can often deliver better returns for the same level of risk.
4. **Reduces Emotional Investing**
   It helps keep investors calm during market swings, because not everything drops at once.

How to Achieve Diversification

1. **Across Asset Classes**
   - Equities (stocks)
   - Fixed Income (bonds)
   - Cash or equivalents
   - Real Assets (real estate, commodities)
   - Alternatives (private equity, hedge funds)
2. **Within Asset Classes**
   - For example: Different sectors, company sizes, and regions within stocks.
3. **Geographic Diversification**
   - Include both domestic and international exposure.
4. **Investment Style & Strategy**
   - Blend of growth vs. value, active vs. passive, income vs. capital gains.
5. **Avoid Overconcentration**
   - No single holding should dominate your portfolio unless it’s by choice (e.g. concentrated bet with conviction + hedges).

Common Diversification Pitfalls

- **False diversification**: Holding many assets that are still highly correlated (e.g. multiple tech stocks).
- **Overdiversification**: Spreading too thin, which can dilute performance and make monitoring difficult.
- **Neglecting rebalancing**: Portfolios drift over time. Periodic rebalancing maintains intended diversity.

Diversification
The strategy of spreading investments to reduce risk.
Why It Matters
Reduces overall portfolio risk
Helps smooth out returns
Provides protection against market volatility
How to Diversify
Mix asset classes (stocks, bonds, real estate, etc.)
Diversify within each asset class
Include exposure to different sectors and regions
Avoid overconcentration in single investments
Common Pitfalls
Inadequate portfolio rebalancing
Ignoring correlations between assets
Overdiversifying and reducing returns

4-13 Performance

What Is Investment Performance?

Performance refers to the return generated by an investment over a period of time, including:

- Capital Gains – increase in asset value
- Income – dividends, interest, rental income
- Total Return – combined capital gains + income, often compared to benchmarks

It's usually measured as a percentage, annualized for comparison.

Why Performance Matters

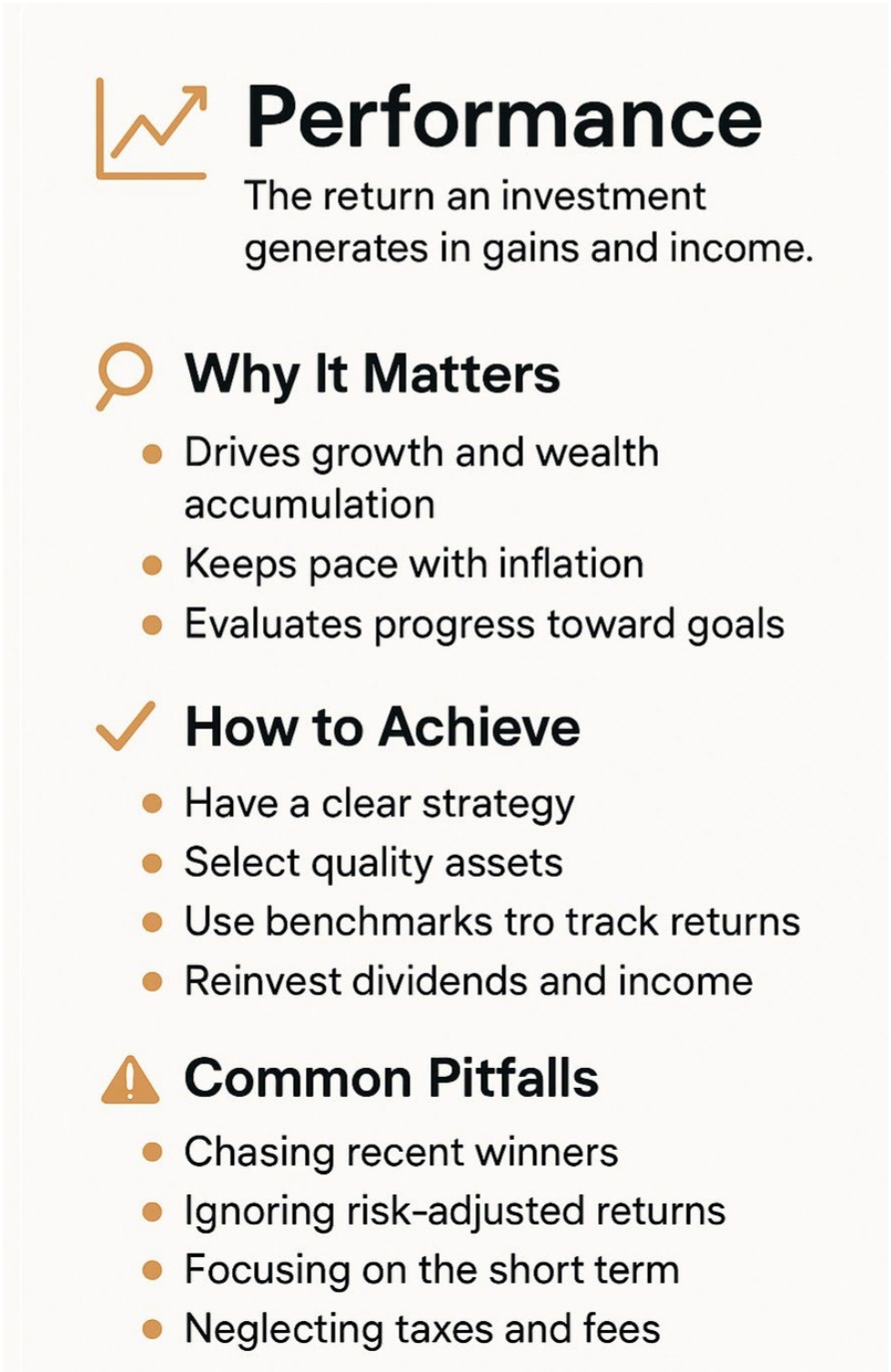
1. **Drives Wealth Growth**
   Strong, compounding returns are essential for reaching financial goals.
2. **Keeps You Ahead of Inflation**
   Beating inflation protects your purchasing power over time.
3. **Measures Strategy Effectiveness**
   Helps assess if your portfolio, fund manager, or strategy is working as expected.
4. **Informs Rebalancing or Switching**
   Lagging performance may indicate it's time to reassess or pivot.

How to Achieve Strong Performance

1. **Have a Clear Investment Strategy**
   Stick to an approach that matches your goals and risk tolerance (e.g., growth, income, balanced).
2. **Select Quality Assets**
   Favor fundamentally strong companies, funds, or properties with track records and upside potential.
3. **Use Benchmarks**
   Compare your portfolio against appropriate benchmarks (S&P 500, bond indexes, etc.) to gauge relative performance.
4. **Reinvest Returns**
   Reinvest dividends and interest to harness the power of compounding.
5. **Avoid Performance Chasing**
   Don't jump into recent winners blindly—look for sustainable long-term drivers.
6. **Manage Risk Actively**
   Better performance often comes not from wild bets but from protecting against big losses.

Common Performance Mistakes

- Focusing only on short-term gains
- Ignoring risk-adjusted returns
- Not accounting for taxes and fees
- Confusing luck with skill
- Overreacting to recent performance trends



4-14 Risk

What Is Investment Risk?

Risk is the possibility of losing money or not achieving your expected return. It's not just about market crashes—it includes:

- Market risk (price volatility)
- Credit risk (default)
- Liquidity risk (can't exit)
- Inflation risk (loss of purchasing power)
- Concentration risk (overexposure to one asset)

In essence, risk is uncertainty—and every investment carries some.

Why Risk Management Is Crucial

1. **Preserves Capital**
   Avoiding big losses is more important than chasing big gains.
2. **Supports Long-Term Growth**
   Stable, risk-adjusted returns compound better over time.
3. **Reduces Emotional Decisions**
   A well-managed portfolio helps you stay calm in turbulent markets.
4. **Aligns Strategy with Goals**
   Risk should match your objectives and timeline—not someone else's.

How to Manage Investment Risk

1. **Know Your Risk Tolerance**
   Be honest about how much volatility you can stomach—emotionally and financially.
2. **Diversify Wisely**
   Spread risk across asset classes, sectors, and regions.
3. **Use Position Sizing**
   Never bet too much on a single idea—limit how much you put into any one asset.
4. **Have an Exit Plan**
   Know when you'll take profits or cut losses.
5. **Use Stop-Losses and Hedging Tools** (if active)
   Especially in volatile markets or for tactical plays.
6. **Avoid FOMO Investing**
   Chasing hype increases your exposure to high, uncalculated risk.

7. **Rebalance Regularly**

   Your portfolio can drift into higher-risk zones over time—pull it back in line.

Common Mistakes

- Confusing risk with volatility (not all volatility is bad)
- Underestimating how fast losses compound
- Ignoring tail risks or black swan events
- Taking more risk than needed to meet your goals
- Overconfidence in high-return environments

RISK
The possibility of losing money or not achieving the expected return.
WHY IT'S IMPORTANT
• Preserves capital
• Supports long-term growth
• Reduces emotional decisions
• Aligns strategy with goals
HOW TO MANAGE
• Know your risk tolerance
• Diversify wisely
• Use position sizing
• Have an exit plan
• Use stop-losses, hedging
• Rebalance regularly
COMMON MISTAKES
• Confusing risk with volatility
• Underestimating potential losses
• Ignoring black swan events

4-15 Time

What Does "Time" Mean in Investing?

Time refers to your investment horizon—how long you plan to hold an asset before needing to access the money.

Time affects:

- Your risk tolerance
- The types of assets you should hold
- How you deal with volatility

Why Time Matters

1. **Time Reduces Risk**
   The longer your horizon, the more short-term volatility you can afford to ride out.
2. **Enables Compounding**
   Time + consistency = exponential growth through reinvested gains.
3. **Shapes Strategy**
   Short-term = focus on liquidity and safety
   Long-term = growth and risk-taking are more viable
4. **Prevents Emotional Mistakes**
   Knowing your timeline helps avoid panic selling in downturns.

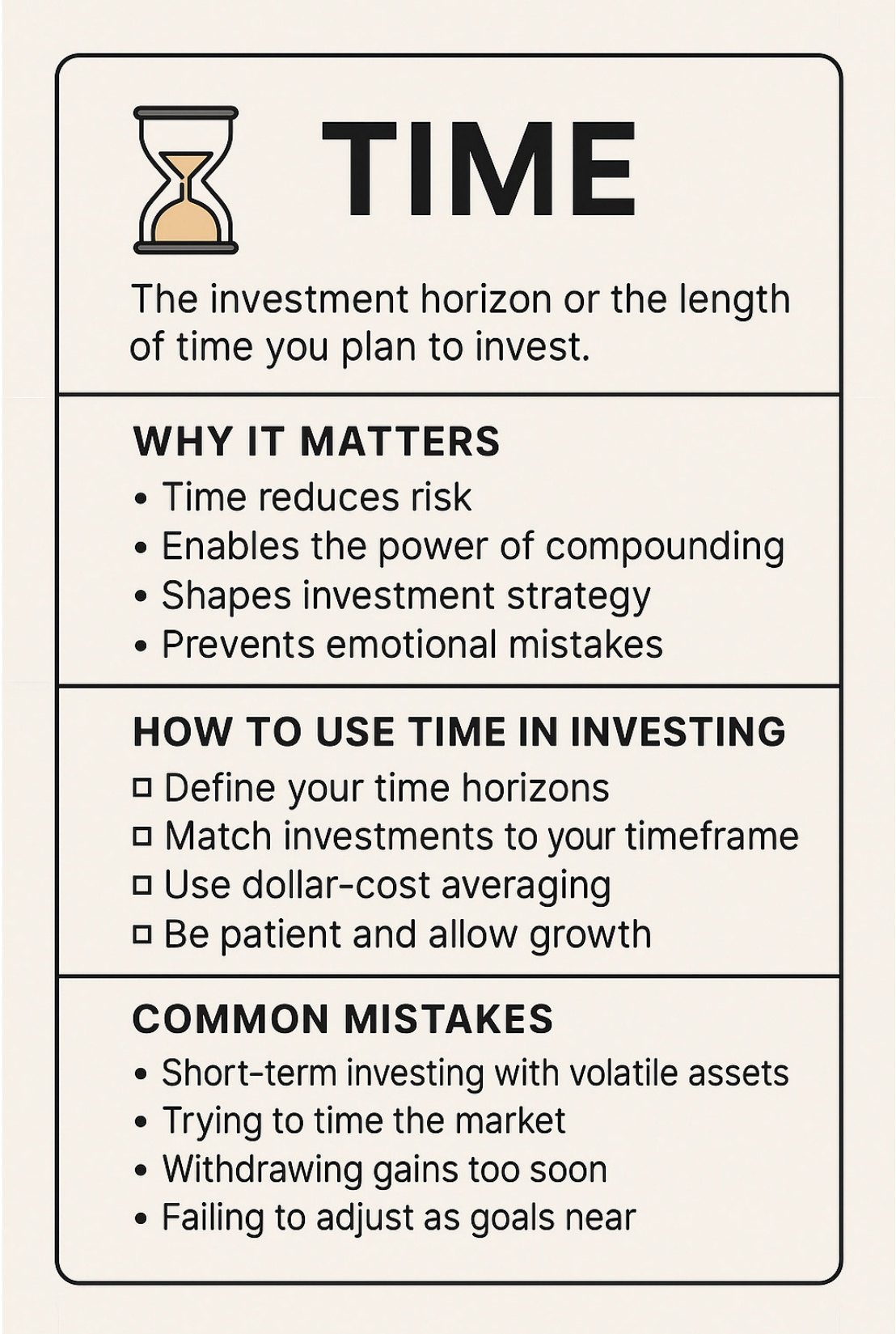
How to Use Time in Investing

1. **Define Your Time Horizons**
   - Short (0–2 years): safety, liquidity
   - Medium (2–5 years): balanced, mixed-risk
   - Long (5+ years): growth, equities, real estate
2. **Match Investments to Timeframe**
   Don't lock funds into volatile assets if you'll need them soon.
3. **Use Dollar-Cost Averaging**
   Spread investments over time to lower entry risk in volatile markets.
4. **Revisit & Adjust**
   As goals near, shift to safer assets (e.g., pre-retirement glide path).
5. **Be Patient**
   Great investments need time to work. Don't interrupt compounding too early.

Common Mistakes

- Investing short-term money in high-volatility assets

- Trying to time the market instead of spending time in the market
- Ignoring compounding by withdrawing gains early
- Not adjusting portfolios as time horizons change


TIME
The investment horizon or the length of time you plan to invest.
WHY IT MATTERS
• Time reduces risk
• Enables the power of compounding
• Shapes investment strategy
• Prevents emotional mistakes
HOW TO USE TIME IN INVESTING
Define your time horizons
Match investments to your timeframe
Use dollar-cost averaging
Be patient and allow growth
COMMON MISTAKES
• Short-term investing with volatile assets
• Trying to time the market
• Withdrawing gains too soon
• Failing to adjust as goals near

4-16 Goals

What Are Investment Goals?

Investment goals are specific financial targets you're aiming for. They guide why you're investing, how much you need, and when you'll need it.

Examples:

- Retire at 60 with $1M
- Buy a home in 5 years
- Fund a child's education
- Generate passive income by 2030

Why Goals Matter

1. **Create a Roadmap**
   Goals define your destination—and help shape the journey.
2. **Guide Risk and Asset Choices**
   Short-term goals need safer assets; long-term goals can handle more volatility.
3. **Provide Motivation & Discipline**
   Clear goals help you stay focused, even in market dips.
4. **Enable Performance Tracking**
   You can measure progress and adjust your strategy accordingly.

How to Set and Align Goals

1. **Be SMART**
   - **S**pecific
   - **M**easurable
   - **A**chievable
   - **R**ealistic
   - **T**ime-bound
2. **Prioritize Your Goals**
   Not all goals are equal. Know which ones come first or need more funding.
3. **Assign Time Horizons**
   - Short-term (<2 years): capital preservation
   - Medium-term (2–5 years): balanced growth/safety
   - Long-term (5+ years): higher growth
4. **Match Strategy to Each Goal**
   Build mini-portfolios or asset mixes that fit each goal's risk/time needs.

5. **Review and Adjust**

   Life changes—so should your investment goals and plans.

Common Mistakes

- Investing without a clear reason or timeline
- Using one-size-fits-all strategies
- Ignoring how life events affect goals
- Focusing only on returns, not purpose
- Not revisiting or tracking progress

GOALS
WHY THEY MATTER
• Define your investing purpose
• Determine risk, asset mix
• Keep you motivated and on track
• Enable progress checks
HOW TO SET AND ALIGN THEM
• Be SMART
• Prioritize your goals
• Assign time horizons
• Match strategy to each goal
• Review regularly
COMMON MISTAKES
• Investing without a plan
• One-size-fits-all approach
• Failing to revisit goals
• Focusing only on returns

4-17 Costs

What Do Costs Mean in Investing?

Costs are the fees, charges, and taxes that reduce your net investment returns. They're often overlooked—but over time, even small costs can compound into large losses.

Types include:

- **Fund Fees** (expense ratios, management fees)
- **Trading Costs** (commissions, bid-ask spread, slippage)
- **Taxes** (capital gains, dividend tax)
- **Account Fees** (custody, advisory, platform)

Why Costs Matter

1. **Directly Reduce Returns**
   A 1% annual fee might not sound like much, but over 30 years it can reduce your final wealth by 20%–30%.
2. **Compounding Works Both Ways**
   Just as returns compound, **costs compound against you**.
3. **Hard to Outperform When Costs Are High**
   Especially true in low-return environments—fees become a bigger share of performance.
4. **Controllable Variable**
   Unlike market returns, you *can* control what you pay.

How to Keep Costs Low

1. **Use Low-Cost Index Funds or ETFs**
   They often outperform higher-cost active funds after fees.
2. **Avoid Excessive Trading**
   Active trading = more commissions, spreads, and tax events.
3. **Mind the Tax Impact**
   Use tax-advantaged accounts and be strategic with asset placement.
4. **Compare Expense Ratios**
   Always review fund fees—even among similar options.
5. **Question Advisory Fees**
   Make sure you're getting value for advice or portfolio management.
6. **Automate to Save**
   Many platforms offer free auto-investing or no-commission trades.

Common Mistakes

- Not noticing or comparing fund expenses
- Overtrading due to emotion or news
- Ignoring the long-term impact of “just 1%”
- Holding tax-inefficient investments in taxable accounts
- Paying for services you don’t use or need

Costs
Meaning, Importance, How to Achieve
Why They Matter
• Directly decrease your returns
• Compounding magnifies their impact
• High costs are hard to outperform
• One of the few factors you can control
How to Keep Them Low
• Use low-cost index funds and ETFs
• Minimize excessive trading
• Consider tax implications
• Compare expense ratios
• Reevaluate advisor fees
• Automate to save
Common Mistakes
• Overlooking fund fees
• Frequent buying and selling
• Downplaying the long-term impact

4-18 Consistency

What Does Consistency Mean in Investing?

Consistency means sticking to your strategy, process, and principles—over time and through market ups and downs. It's about reliability in behavior, not chasing short-term wins or reacting emotionally.

Why Consistency Matters

1. **Builds Long-Term Success**
   Investing is a marathon. Staying consistent lets compounding work its magic.
2. **Reduces Emotional Errors**
   A steady approach helps avoid panic selling, FOMO buying, and market timing traps.
3. **Supports Strategic Discipline**
   Rebalancing, goal-checking, and steady contributions outperform impulsive decisions.
4. **Maximizes Compounding**
   Skipping periods or jumping in and out breaks the compounding chain.

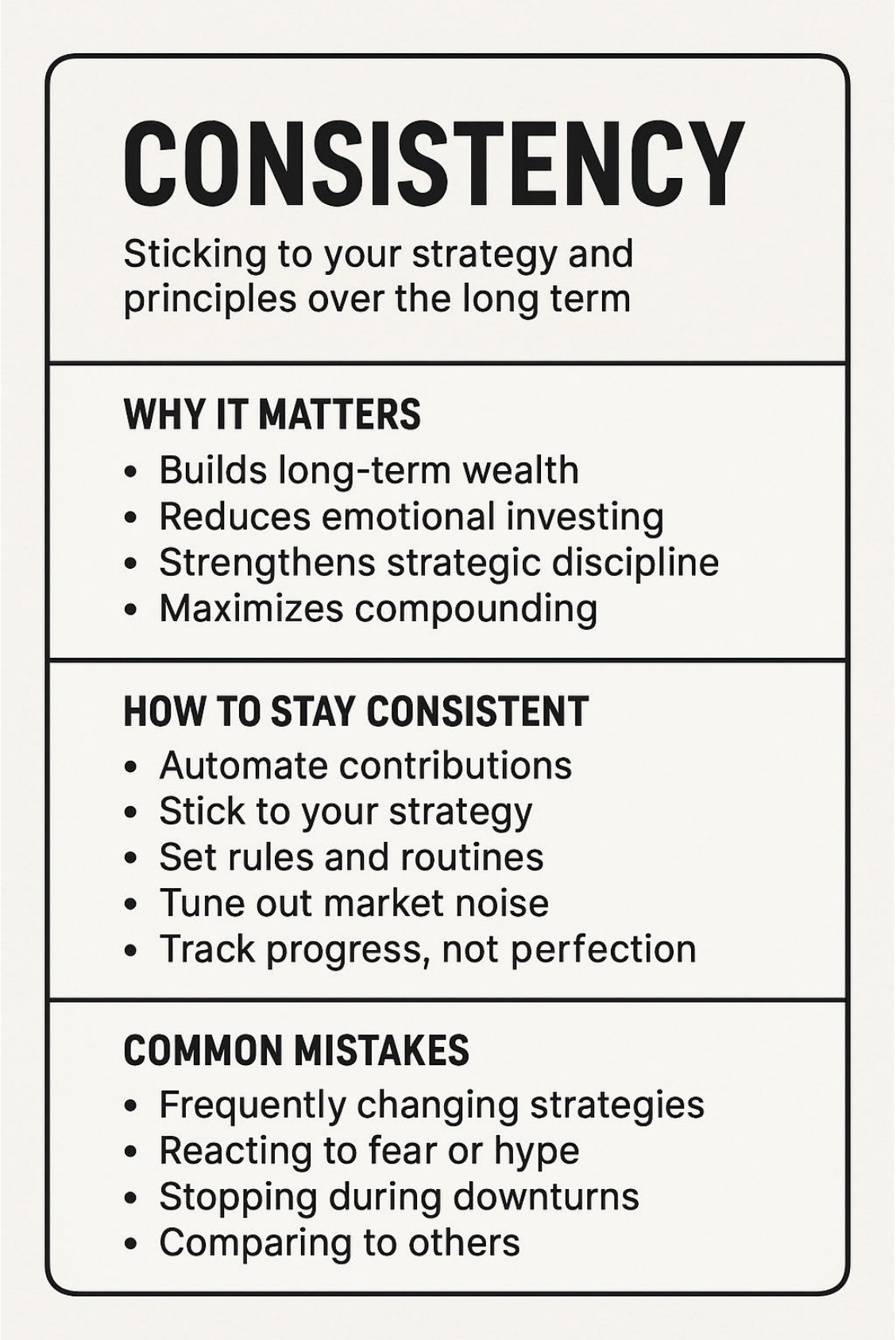
How to Stay Consistent

1. **Automate Contributions**
   Use recurring transfers to invest steadily (e.g., monthly).
2. **Stick to Your Strategy**
   Whether it's growth, income, value, or passive indexing—stay aligned with your plan.
3. **Set Rules & Routines**
   Rebalance regularly, review annually, and avoid unnecessary tweaks.
4. **Ignore Market Noise**
   News cycles and hype can derail you—filter them out.
5. **Track Progress, Not Perfection**
   Focus on long-term outcomes, not short-term swings.
6. **Celebrate Discipline**
   Reward yourself for *not* panicking or reacting emotionally.

Common Mistakes

- Frequently switching strategies or funds
- Letting fear or greed override the plan
- Stopping investments during downturns
- Comparing your results constantly with others

- Being active when patience would pay more


CONSISTENCY
Sticking to your strategy and principles over the long term
WHY IT MATTERS
• Builds long-term wealth
• Reduces emotional investing
• Strengthens strategic discipline
• Maximizes compounding
HOW TO STAY CONSISTENT
• Automate contributions
• Stick to your strategy
• Set rules and routines
• Tune out market noise
• Track progress, not perfection
COMMON MISTAKES
• Frequently changing strategies
• Reacting to fear or hype
• Stopping during downturns
• Comparing to others

4-19 Simplicity

What Does Simplicity Mean in Investing?

Simplicity is about keeping your investment approach clear, understandable, and manageable.

“If you can’t explain it to a 12-year-old, you may not fully understand it yourself.”

It means using straightforward strategies, transparent instruments, and minimal complexity—no fancy jargon or overengineering.

Why Simplicity Matters

1. **Reduces Mistakes**
   Complexity hides risks, makes monitoring harder, and increases room for error.
2. **Improves Clarity and Confidence**
   Simpler portfolios are easier to stick with during volatility.
3. **Lowers Costs**
   Complex strategies often involve higher fees, active management, and hidden charges.
4. **Boosts Long-Term Returns**
   Simple strategies like low-cost index investing often outperform complicated ones over time.

How to Keep Investing Simple

1. **Use Broad Index Funds or ETFs**
   Capture entire markets with one product.
2. **Limit the Number of Holdings**
   A few well-chosen funds can give all the diversification you need.
3. **Avoid Frequent Trading or Overengineering**
   Stick to a rules-based system. Don’t chase fads or micromanage.
4. **Automate When Possible**
   Regular contributions, dividend reinvestment, and rebalancing can all be automated.
5. **Stick to What You Understand**
   If you don’t get it, don’t buy it.
6. **Have a Written Plan**
   Simplicity = clarity. A documented strategy prevents overreaction.

Common Mistakes

- Over-diversifying into similar assets
- Chasing complex products with hidden fees
- Confusing “active” with “smart”
- Letting ego or trends lead instead of logic
- Believing more effort = better results (not always true)

4-2 Putting It All Together

4-21 Investment Pyramid

Explanation:

- Base (Liquidity, Diversification): These ensure access and protection.
- Middle (Performance, Risk, Time, Goals): This is where your strategy gets shaped.
- Top (Consistency, Simplicity): These keep the system running and sustainable.

4-22 Decision Tree

DECISION TREE:
MAKING AN INVESTMENTT DECISION
NEW INVESTMENT IDEA
Is it diversified
Reject or rethink
Does it have solid performance potential?
Pass or investigate more
Are the risks clearly defined and manageable?
No – risky
Does it align with your time horizon?
Mismatch with goals
Does it serve a specific goal?
Avoid aimless investing
Are the costs reasonable (fees, taxes, etc,)?
Hidden drag on returns
Can you stick with it consistently?
Avoid temptation traps
Is the strategy simple and understandable
Complexity hides trouble
YES → Consider Investing

4-23 Checklist

Golden Rules Investment Checklist

- [ ] **Liquidity**
  Can I sell or exit this investment easily if needed?
- [ ] **Diversification**
  Does this add balance to my overall portfolio, or is it overlapping?
- [ ] **Performance**
  Is there a strong case for solid returns (historical or expected)?
- [ ] **Risk Management**
  Do I understand the risks, and are they within my acceptable limits?
- [ ] **Time**
  Does this fit my investment time horizon (short, medium, long term)?
- [ ] **Goals**
  Is this investment aligned with a specific goal (e.g, retirement, income, growth)?
- [ ] **Consistency**
  Can I stick with this investment strategy consistently, even in tough times?
- [ ] **Keep it Simple**
  Do I fully understarnd how this investment works?

Chapter 5

How to Engage

5-1 Day Trading

Engaging in the stock market offers private investors several avenues, each with distinct characteristics, risk profiles, and potential returns. Understanding these options is crucial for aligning investment strategies with personal financial goals and risk tolerance.

Common Avenues for Private Investors:

1. **Long-Term Investing:** Involves purchasing stocks or other securities to hold for extended periods, often years or decades. This strategy aims to benefit from the overall growth of the market and compound interest over time.
2. **Swing Trading:** Entails holding positions for several days to weeks to capitalize on expected upward or downward market shifts. Swing traders rely on technical analysis to identify potential entry and exit points.
3. **Day Trading:** Involves buying and selling financial instruments within the same trading day, with all positions closed before the market closes. Day traders seek to profit from short-term price movements and typically do not hold positions overnight.

Is Day Trading a Viable Strategy?

Day trading is often perceived as a quick path to profits, but empirical evidence suggests otherwise. The success rate among day traders is notably low:

- **High Failure Rates:** Studies indicate that a significant majority of day traders incur losses. For instance, research from the University of California found that more than 80% of day traders lose money over a typical six-month period. Haas
- **Low Long-Term Success:** Only about 1% of day traders are able to achieve consistent profitability over a five-year span. Quantified
- **Attrition Rates:** Approximately 40% of day traders quit within a month, and only 13% continue after three years. Quantified

Scientific Research Findings:

Academic studies further illuminate the challenges of day trading:

- **Limited Profitability:** A study analyzing Taiwanese day traders revealed that about twice as many traders lose money as those who make profits, with only approximately 20% being more than marginally profitable. https://tinyurl.com/34ddwzv5 Haas
- **Experience Doesn't Guarantee Success:** Research indicates that even with increased experience, many day traders do not improve their profitability, suggesting inherent difficulties in the practice. Haas

Conclusion:

While day trading is a legal and accessible avenue for private investors, the statistical evidence and academic research highlight its high-risk nature and low probability of consistent success. Private investors should carefully assess their financial goals, risk tolerance, and the substantial commitment required before engaging in day trading. Exploring other investment strategies, such as long-term investing or swing trading, may offer more sustainable paths to achieving financial objectives.

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5-2 Stock Picking

Stock picking involves selecting individual stocks with the expectation that they will outperform the broader market.

Is Stock Picking a Viable Strategy for Private Investors?

While stock picking can be appealing, empirical evidence suggests that consistently outperforming the market through this method is challenging:

- **Low Success Rates:** Research indicates that only about 20% of individual stocks outperform the market over extended periods. Dimensional
- **High Underperformance:** A significant proportion of individual stocks underperform the market, with many experiencing substantial declines in value. White
- **Market Efficiency:** The efficient market hypothesis suggests that all known information is quickly reflected in stock prices, making it difficult for individual investors to gain an edge through stock picking. Investopedia

Scientific Research Findings:

Academic studies further highlight the challenges associated with stock picking:

- **Performance Persistence:** Evidence suggests that past performance of individual stocks is not a reliable predictor of future success, indicating that stock picking based on historical performance may not yield consistent results.
- **Behavioral Biases:** Individual investors are often influenced by behavioral biases such as overconfidence and regret, leading to suboptimal trading decisions and underperformance. Investopedia

Conclusion:

While stock picking offers the potential for significant gains, the statistical evidence and academic research highlight its high-risk nature and low probability of consistent success for private investors. Alternative strategies, such as investing in diversified index funds or adopting evidence-based investment approaches, may provide more reliable paths to achieving financial objectives.

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5-3 Market Timing

Market timing involves attempting to predict future market movements to buy low and sell high. Understanding the viability of market timing is crucial for investors considering this approach.

Is Market Timing a Viable Strategy for Private Investors?

Market timing is challenging and often results in underperformance compared to passive investment strategies:

- **Difficulty in Accurate Predictions:** Consistently forecasting market movements is exceedingly difficult, even for professional investors. Investopedia

- **Risk of Missing Key Market Days:** Attempting to time the market can lead to missing periods of substantial gains. For instance, missing just a few of the best-performing days can significantly reduce long-term returns. Investopedia

Scientific Research Findings:

Academic studies further highlight the pitfalls of market timing:

- **Low Success Rates:** Research indicates that the overall odds of succeeding with a market timing strategy are low, with many investors underperforming compared to those who adopt a buy-and-hold approach. bbh.com
- **Behavioral Biases:** Investors attempting to time the market may fall prey to emotional decisions, such as panic selling during downturns or excessive optimism during upswings, leading to poor investment outcomes.

Conclusion:

While the allure of market timing is understandable, the evidence suggests that it is a high-risk strategy with a low probability of consistent success for private investors. A more prudent approach involves adopting a long-term investment strategy, focusing on asset allocation, diversification, and regular portfolio rebalancing to achieve financial goals.

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5-4 Derivatives

Understanding what derivatives are, their potential benefits, and the associated risks is crucial before considering this approach.

What Are Derivatives?

Derivatives are financial contracts whose value is derived from an underlying asset, such as stocks, bonds, commodities, or market indices. Common types of derivatives include futures, options, swaps, and forwards. These instruments can be traded on exchanges or over-the-counter (OTC) and are often used for hedging risks or speculating on price movements.

Is Trading Derivatives a Viable Strategy for Private Investors?

While derivatives can offer opportunities for hedging and potential profits, they come with significant risks, especially for private investors:

- **Complexity and Leverage:** Derivatives are complex instruments that often involve leverage, amplifying both potential gains and losses. This complexity can make them challenging for individual investors to manage effectively.
- **High Loss Rates Among Retail Investors:** Studies have shown that a substantial majority of retail investors incur losses when trading derivatives. For instance, research indicates that approximately 95% of all traders fail to achieve profitability, with many losing money. Trading
- **Market Efficiency and Professional Competition:** The derivatives market is highly competitive, with professional and institutional investors often having access to more information and sophisticated trading tools, making it difficult for private investors to compete successfully.

Scientific Research Findings:

Academic studies further highlight the challenges associated with derivatives trading for private investors:

- **Underperformance:** Research analyzing trading behaviors has found that individual investors often underperform in derivatives markets, with a significant portion experiencing losses. Trading
- **Behavioral Biases:** Individual investors are susceptible to behavioral biases, such as overconfidence and the disposition effect, leading to suboptimal trading decisions and increased losses in derivatives trading.

Conclusion:

While derivatives can serve as useful tools for hedging and offer opportunities for profit, they are complex and carry substantial risks, particularly for private investors. The statistical evidence and academic research suggest that the success rate among private investors in derivatives trading is low. Therefore, private investors should approach derivatives with caution, thoroughly educate themselves, and consider whether such instruments align with their investment objectives and risk tolerance. Alternative strategies, such as long-term investing in diversified portfolios, may offer more sustainable paths to achieving financial goals.

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5-5 Robo Investing

Avenues for Private Investors to Engage in the Stock Market

Private (retail) investors today have several ways to get involved in the stock market:

1. **Self-Directed Investing**
    - Through platforms like Vanguard, Fidelity, Schwab, E*TRADE, or Robinhood.
    - You choose and manage your own portfolio: stocks, ETFs, mutual funds, etc.
2. **Traditional Financial Advisors**
    - Human advisors provide customized plans.
    - Higher fees (typically 1% of AUM), but often bundled with estate or tax planning.
3. **Robo-Advisors (Robo Investing)**
    - Automated portfolio management based on algorithms.
    - Lower fees (usually 0.25–0.50%), good for hands-off investors.
    - Examples: Betterment, Wealthfront, Schwab Intelligent Portfolios, Vanguard Digital Advisor.
4. **Managed Funds or Target-Date Funds**
    - You invest in a fund that's managed by professionals or adjusted by your retirement horizon.
5. **Thematic Platforms & Social Investing**
    - Newer platforms like eToro allow social trading or theme-based investing.

What is Robo-Investing?

Robo-investing is the use of automated algorithms to manage your investment portfolio. You:

- Fill out a questionnaire (risk tolerance, goals, timeline),

- The platform builds a diversified ETF portfolio for you,
- It automatically rebalances, reinvests dividends, and may harvest tax losses.

It's based on Modern Portfolio Theory and generally aims to match risk-adjusted returns rather than beat the market.

Success Rate & Statistics

- Assets Under Management (AUM)

- As of 2024, robo-advisors manage over $1.5 trillion globally, and growing steadily.

- Performance

- Studies show robo-advisors often perform as well or better than the average human financial advisor net of fees.
- They tend to mirror market returns minus a small fee (like passive index investing).

- Costs

- Fees: ~0.25% vs. ~1.0% for human advisors.
- Often no minimums or low minimums (e.g. $500–$3,000).

Scientific Research & Findings:

Several academic and industry studies have analyzed robo-advisors:

1. Performance vs. Human Advisors

- *Fein (2022, CFA Institute)*: Robo-advisors provided comparable net returns but lacked personal touch for complex needs.
- *Salo & Haapaniemi (2020)*: Robo-advisors in Finland performed slightly better than traditional advisors on average due to lower fees.

2. Behavioral Benefits

- *Gallagher & Looi (2020)*: Robos reduce investor emotion-driven mistakes (like panic selling).
- Automated rebalancing and consistent asset allocation = improved investor discipline.

3. Suitability

- Robo-advisors are best for:
    - New investors,
    - People with basic financial needs,
    - Those wanting low-cost, passive portfolios.

Conclusion: Is Robo-Investing the Way?

- Pros

- Low cost, easy to use
- Diversification and automation
- Emotion-free, rules-based
- Good for most long-term investors

- Cons

- Limited human advice
- Can’t handle complex needs (tax planning, estate, inheritance)
- Quality varies by platform

Verdict:

For 90% of private investors, especially those focused on long-term, simple, passive investing, robo-advisors are a smart, cost-effective choice. They’re not perfect, but for simplicity, discipline, and diversification—they deliver.

Comparison Table: Top Robo-Advisors (2025)

Platform	Fees (Mgmt)	Account Min.	Tax Loss Harvesting	Rebalancing	Notable Features
Betterment	0.25%	$0	Yes	Auto	Goal tracking, human advice (extra)
Wealthfront	0.25%	$500	Yes	Auto	Financial planning tools
Vanguard Digital	0.20%	$3,000	No	Auto	Uses Vanguard ETFs, solid reputation
Schwab Intelligent	$0 (ETF fee only)	$5,000	No	Auto	No direct fees, cash drag noted
SoFi Automated	0.00%	$0	No	Auto	Free, beginner-friendly
M1 Finance	0.00%	$100	No (manual)	Manual	Customizable "pies", not true robo

Notes:

- Tax Loss Harvesting (TLH) is ideal for taxable accounts; it's like “selling at a loss” for tax benefits.
- Rebalancing ensures your asset allocation stays on track automatically.

Beginner’s Roadmap to Start with Robo-Investing

1. Define Your Goals

- Retirement? Down payment? General wealth building?
- Time horizon (e.g., 5 years, 20 years)?
- Risk tolerance: conservative, balanced, or aggressive?

2. Pick a Robo-Advisor

- Choose based on:
    - Cost
    - Features (TLH, human advice)
    - Ease of use
    - Reputation

Tip: If you're starting small, Betterment or SoFi are ideal.

3. Open an Account

- Choose the account type:
    - Taxable Brokerage
    - IRA / Roth IRA
    - Joint Account

4. Answer the Questionnaire

- Robo-advisors ask:
    - How long do you plan to invest?
    - How much volatility can you handle?
    - What’s your income?

This generates a personalized portfolio, often ETF-based, diversified by risk level.

5. Fund Your Account

- Connect your bank and transfer funds.
- Many robos allow auto-deposits for dollar-cost averaging.

6. Let It Work

- The robo will:
    - Invest in low-cost ETFs
    - Rebalance automatically
    - Monitor your goals

7. Revisit Annually

- Adjust your risk level or add goals.
- Most platforms offer easy dashboards and alerts.

Pro Tip:

Set up auto-contributions and leave it alone. The real magic of robo-investing is consistency + compound growth + low fees.

Here's a simple starter portfolio example built using the style of most robo-advisors. It assumes a balanced investor profile (medium risk tolerance, long-term goals like retirement or general wealth growth).

Starter Portfolio (Balanced Risk Profile)

Asset Class	ETF Example	Allocation	Expected Return (Annualized)	Notes
U.S. Stocks	VTI (Total U.S.)	35%	~7–9%	Core engine of growth
International Stocks	VXUS (Intl)	15%	~6–8%	Diversifies away from U.S. risk
U.S. Bonds	BND (Aggregate)	30%	~2–4%	Provides stability and income
International Bonds	BNDX (Intl Bonds)	10%	~2–3%	Extra diversification, low yield
Real Assets (Optional)	GLDM or VNQ	5%	~5–7%	Hedge (gold or real estate)
Cash or Short-Term	BIL (T-Bills)	5%	~3–5%	Liquidity buffer

Blended Expected Return

If you weight the returns:

- Approximate expected return: ~5.5–6.5% annually
- Standard deviation: Moderate (~8–10%)
- Suited for long-term investors with mild to moderate volatility tolerance.

Why This Works for Beginners

- Diversification across geography, asset class, and volatility.
- Low-cost ETFs that robo-advisors already use.
- Set it and forget it – ideal for passive investing.
- Return profile aligned with long-term wealth-building, retirement planning.

Simulated Performance (2005–2025)

Using blended estimates from historical data and academic sources for the ETFs:

Component	Allocation	Avg Annual Return (Est.)	Volatility (Est.)
VTI (U.S. Stocks)	35%	~9.5%	~15%
VXUS (Intl Stocks)	15%	~7.5%	~16%
BND (U.S. Bonds)	30%	~3.8%	~4%
BNDX (Intl Bonds)	10%	~3.5%	~5%
GLDM (Gold)	5%	~6.8%	~15%
BIL (Short-Term Bills)	5%	~2.2%	~1%

Blended Portfolio Metrics

- Annualized Return (Est.): ~6.1–6.4%
- Annualized Volatility: ~8–9%
- Worst Year: ~-20% (2008 financial crisis)
- Best Year: ~18–20% (2009, 2017 range)

This portfolio balances growth with downside protection, and historically it would have turned $10,000 into $32,000–$36,000 over 20 years.

5-6 Funds

5-61 Mutual Funds

Engaging in the stock market through traditional mutual funds—those bought and sold directly via the issuer—has been a prevalent strategy for private investors. Understanding their structure, performance metrics, and the insights from academic research can help determine their suitability for individual investment goals.

Understanding Traditional Mutual Funds:

Traditional mutual funds pool capital from multiple investors to purchase a diversified portfolio of stocks, bonds, or other securities. They are actively managed by professional fund managers who aim to outperform specific market benchmarks. Investors buy and sell shares of these funds directly through the fund company at the net asset value (NAV) calculated at the end of each trading day.

Performance and Success Rates:

The effectiveness of actively managed mutual funds in delivering superior returns has been extensively studied:

- **Underperformance Relative to Benchmarks:** A significant proportion of actively managed mutual funds fail to consistently outperform their market benchmarks over extended periods. For instance, over a 10-year span, a substantial percentage of U.S. equity mutual funds underperformed the S&P 500 index. Financial Times
- **Persistence of Performance:** Research indicates that mutual funds demonstrating strong performance in one period do not necessarily maintain that performance in subsequent periods. This lack of persistence suggests challenges in selecting consistently high-performing funds based on past results.

Findings from Academic Research:

Academic studies provide further insights into mutual fund performance:

- **Impact of Fees on Returns:** Higher management fees and expenses associated with actively managed mutual funds can erode net returns to investors. The compounding effect of these costs over time can significantly diminish the potential benefits of active management.
- **Investor Behavior and Decision-Making:** Studies have observed that mutual fund investors often base their investment decisions on past performance, despite evidence suggesting limited persistence. This behavior can lead to suboptimal investment choices and highlight the importance of considering factors beyond historical returns. Haas

Conclusion:

While traditional mutual funds offer private investors a means to access diversified portfolios managed by professionals, empirical evidence raises questions about their ability to consistently outperform passive investment strategies, especially after accounting for fees and expenses. Investors should carefully evaluate their investment objectives, risk tolerance, and the cost implications of mutual fund investments. Considering alternative strategies, such as low-cost index funds or ETFs, may provide more consistent and cost-effective avenues for achieving long-term financial goals.

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5-62 ETF

Engaging in the stock market through Exchange-Traded Funds (ETFs) has become an increasingly popular strategy for private investors. Understanding the structure, benefits, and empirical performance of ETFs can help determine their suitability within an investment portfolio.

Understanding ETFs:
ETFs are investment funds that trade on stock exchanges, similar to individual stocks. They typically aim to replicate the performance of a specific index, sector, commodity, or asset class. ETFs combine the diversification benefits of mutual funds with the trading flexibility of stocks, allowing investors to buy and sell shares throughout the trading day at market-determined prices.

Performance and Success Rates:
The effectiveness of ETFs as an investment vehicle has been the subject of various studies:

- **Comparison with Mutual Funds:** Research indicates that ETFs often have lower expense ratios compared to mutual funds, which can contribute to better net performance over time. Additionally, the tax efficiency of ETFs, stemming from their unique creation and redemption processes, may result in fewer taxable events for investors. Investopedia
- **Market Tracking and Volatility:** While many ETFs successfully track their underlying indices, some studies have found that certain ETFs exhibit higher volatility and may underperform in terms of risk-adjusted returns. For instance, a study by Robeco reported that 60% of ETFs underperformed the market, and 80% exhibited higher volatility. Robeco

Findings from Academic Research:
Academic studies provide further insights into ETF performance:

- **Investor Behavior:** Research suggests that the way investors utilize ETFs can impact portfolio performance. A study highlighted that investors who actively trade ETFs may experience decreased performance due to poor timing and selection decisions. SSRN Alpha

- **Portfolio Diversification:** ETFs offer a convenient means for investors to achieve diversification across various asset classes and sectors, which can help in managing risk and potentially enhancing returns over the long term.

Conclusion:
ETFs present private investors with a flexible and cost-effective avenue to engage in the stock market. Their benefits include lower expense ratios, tax efficiency, and ease of trading. However, the success of investing in ETFs depends on factors such as the specific ETFs chosen, the investor's trading behavior, and alignment with individual financial goals and risk tolerance. As with any investment, thorough research and a clear understanding of the product are essential.

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5-63 Managed Funds

Engaging in the stock market through actively managed funds, such as traditional mutual funds or actively managed ETFs, is a common strategy for private investors. These funds are managed by professionals who aim to outperform market benchmarks through strategic selection and timing of investments.

Performance and Success Rates:
Empirical evidence indicates that actively managed funds often struggle to consistently outperform their passive counterparts:

- **Long-Term Underperformance:** Over a 20-year period, approximately 95% of large-cap actively managed funds underperformed their benchmark indices. Visual
- **Recent Performance:** In 2024, only 13.2% of actively managed mutual funds surpassed the S&P 500, with an average gain of 13.5% compared to the S&P 500's 25% return. Morningstar

- **Active ETFs:** While active ETFs have grown in popularity, they have generally delivered lower average annual returns (12.4%) compared to passive ETFs (13.5%) over the past 15 years, partly due to higher fees. WSJ

Factors Influencing Performance:

Several factors contribute to the challenges faced by actively managed funds:

- **Fees and Expenses:** Higher management fees and operational costs can erode net returns, making it difficult for active funds to outperform benchmarks.
- **Market Efficiency:** The efficient market hypothesis suggests that all available information is already reflected in stock prices, limiting the potential for active managers to consistently identify undervalued securities. Investopedia
- **Performance Persistence:** Past success of active managers does not reliably predict future outperformance, making it challenging for investors to select consistently superior funds. Wikipedia

Conclusion:

While actively managed funds offer the potential for market outperformance, statistical evidence and academic research suggest that they frequently underperform passive investment strategies, especially after accounting for fees and expenses. Private investors should carefully consider their investment objectives, risk tolerance, and the cost implications of active management. Diversified, low-cost passive investment vehicles may provide more consistent and cost-effective avenues for achieving long-term financial goals.

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5-64 Index Funds

Engaging in the stock market through passive index funds, whether via traditional mutual funds or exchange-traded funds (ETFs), has become a widely adopted strategy among private investors. This approach involves investing in funds designed to replicate the performance of specific market indices, offering broad market exposure with minimal active management.

Performance and Success Rates:
Empirical evidence consistently indicates that passive index funds often outperform actively managed funds over extended periods:

- **Long-Term Outperformance:** Over a 20-year span, approximately 90% of active funds have underperformed their passive counterparts, highlighting the efficacy of passive investing strategies. Financial Times
- **Cost Efficiency:** Passive funds typically have lower expense ratios compared to active funds, contributing to better net performance for investors.

Findings from Academic Research:
Academic studies further support the advantages of passive investing: merage.uci.edu

- **Consistency in Returns:** Research indicates that passive funds provide more predictable and stable returns, reducing the uncertainty associated with active management strategies.
- **Market Efficiency:** The efficient market hypothesis suggests that it is challenging for active managers to consistently outperform the market, bolstering the case for passive investing. Investopedia

Conclusion:
For private investors seeking a straightforward, cost-effective, and reliable method to engage with the stock market, passive index funds—whether traditional mutual funds or ETFs—represent a compelling option. The combination of lower fees, broad market exposure, and consistent performance makes them a suitable choice for achieving long-term financial objectives.

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Chapter 6

Portfolio Models

6-1 Definition

What Is an Investment Portfolio?

An investment portfolio is a collection of financial assets owned by an individual, institution, or entity, structured to meet specific financial goals. These assets may include:

- Stocks
- Bonds
- Mutual funds
- Exchange-traded funds (ETFs)
- Real estate
- Commodities
- Cash or cash equivalents

Each investment within a portfolio is chosen based on factors such as risk tolerance, time horizon, investment objectives, and diversification needs.

Key Points:

- A well-constructed portfolio balances risk and return.
- Portfolios can be actively managed (frequent buying/selling) or passively managed (buy-and-hold or index-based).
- Portfolios can be built for growth, income, capital preservation, or a mix of these.
- Diversification within a portfolio helps manage risk by spreading exposure across various asset types and sectors.

6-2 Strategies

Here's an overview of the classic portfolio strategies typically used by private investors. These are time-tested approaches that help balance risk, return, and simplicity, depending on an investor's goals, risk tolerance, and time horizon.

Classic Portfolio Strategies for Private Investors

1. Buy and Hold Strategy

- What it is: Invest in assets and hold them long-term, regardless of short-term market fluctuations.
- Ideal for: Long-term investors who want to benefit from compounding.
- Pros: Low costs, tax-efficient, stress-free.
- Cons: Requires patience and emotional discipline during downturns.

2. Strategic Asset Allocation

- What it is: Set a target mix (e.g., 60% stocks / 40% bonds) and maintain it over time.
- Ideal for: Investors who want a structured, balanced approach.
- Pros: Diversifies risk; helps align portfolio with risk tolerance and goals.
- Cons: May underperform in strongly trending markets if allocation is not adjusted.

3. Tactical Asset Allocation

- What it is: Similar to strategic allocation, but with periodic shifts based on market conditions or forecasts.
- Ideal for: More active investors looking to add an edge.
- Pros: Potentially higher returns if executed well.
- Cons**:** Higher risk, can lead to frequent trading and emotional decisions.

4. Income Investing

- What it is: Focuses on generating steady income through dividends, interest, or rent.
- Ideal for: Retirees or investors seeking cash flow.
- Pros: Generates regular income; can be more stable.
- Cons: Lower capital appreciation; vulnerable to inflation.

5. Growth Investing

- What it is: Emphasizes capital appreciation through high-growth stocks and sectors.
- Ideal for: Younger investors or those with long time horizons.
- Pros: High return potential.
- Cons: Higher volatility and risk.

6. Value Investing

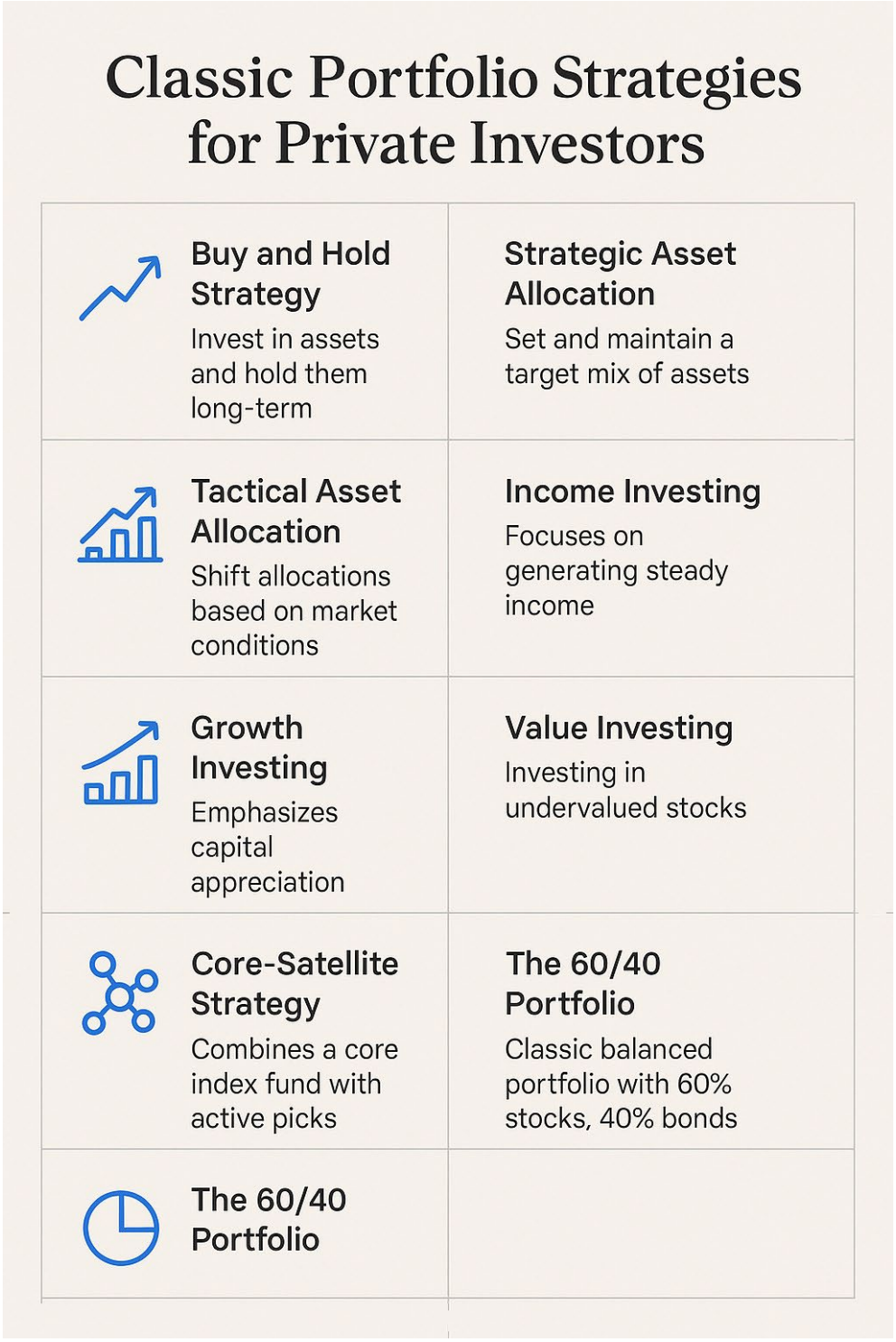
- What it is: Investing in undervalued stocks with strong fundamentals.
- Ideal for: Patient, research-oriented investors.
- Pros: Can outperform over the long term.
- Cons: Requires discipline; may underperform during bull markets.

7. Core-Satellite Strategy

- What it is: Build a “core” portfolio with low-cost index funds, and surround it with “satellites” (active picks or themes).
- Ideal for: Balanced investors seeking diversification and flexibility.
- Pros: Keeps costs low while allowing strategic bets.
- Cons: Requires monitoring and clear rules to avoid drift.

8. The 60/40 Portfolio

- What it is: Classic balanced portfolio with 60% stocks, 40% bonds.
- Ideal for: Moderate-risk investors.
- Pros: Time-tested blend of growth and income.
- Cons: May need adjustment in low-yield or high-volatility environments.

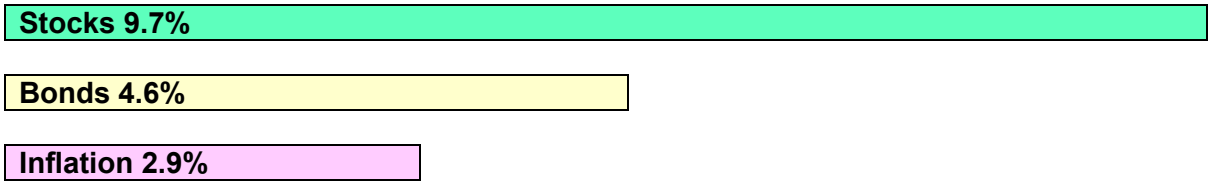

Classic Portfolio Strategies for Private Investors
Buy and Hold Strategy
Invest in assets and hold them long-term
Strategic Asset Allocation
Set and maintain a target mix of assets
Tactical Asset Allocation
Shift allocations based on market conditions
Income Investing
Focuses on generating steady income
Growth Investing
Emphasizes capital appreciation
Value Investing
Investing in undervalued stocks
Core-Satellite Strategy
Combines a core index fund with active picks
The 60/40 Portfolio
Classic balanced portfolio with 60% stocks, 40% bonds
The 60/40 Portfolio

6-3 Keep It Simple

6-31 The Long-Term Approach

6-311 Stocks Beat Them All

USA annualized returns per year 1900-2024 (125 years)



Elroy Dimson, Paul Marsh and Mike Staunton, DMS Database 2025
https://tinyurl.com/bdpuehrj (p. 6)

See also: https://tinyurl.com/4xc3j4vm + https://tinyurl.com/2fazcdtt

6-312 Diversification Helps

Examples:

FTSE Global All Cap Index

Represents the performance of 10,046 constituents in 48 countries: 11 industries, developed and emerging markets, all cap stocks (large, mid, small).

https://tinyurl.com/y36etwdh

ETF: VT

CRSP US Total Market Index

Represents the entire US investable equity market: 3,564 companies, 11 sectors, all cap.

https://tinyurl.com/2ktb37mp

ETF: VTI

S&P 500

Represents 500 leading US companies covering 80% of the available market capitalization: 503 companies, 11 sectors, large cap.

https://tinyurl.com/2x6283vk

ETF: SPY

NASDAQ-100

Represents 100 of the largest domestic and international non-financial companies listed on the Nasdaq stock exchange: 501 companies, 11 industries, large cap

https://tinyurl.com/4hhka7mp

https://tinyurl.com/2ry8xud8

ETF: QQQ

CRSP US Small Cap Index

Represents the US small cap universe: 1,350 companies, 11 sectors, small cap (30 854 – 78 million)

https://tinyurl.com/35ttp9rv

ETF: VB

Bloomberg Global Aggregate Float Adjusted Composite Index

Represents multi-currency bonds, developed and emerging markets, government and corporate issuers.

https://tinyurl.com/4278js4e

ETF: BNDW

MSCI US Investable Market Real Estate 25/50 Index

Represents the US Real Estate market: 156 constituents, Real Estate sector, all cap (large, mid, small).

https://tinyurl.com/ykh32v7p

ETF: VNQ

Sector	ETF	Composition		Ineption	Av. Return/Year
Stocks	VT	9,809	Global Large Cap	06/24/2008	7.45%
	VTI	3,508	US Total Market	05/24/2001	8.57%
	SPY	504	S&P 500	01/22/1993	10.23%

	QQQ	100	Nasdaq-100	03/10/1999	10.03%
	VB	1,364	US Small Cap	01/26/2004	8.76%
Bonds	BNDW	18,172	Global Bond Market	09/04/2018	1.58%
	VGLT	90	US Long-Term Treasury	11/19/2009	2.67%
	TLT	46	US Long-Term Treasury	07/22/2002	3.87%
Gold	GLD		Gold Bullions	11/18/2004	9.57%
Real Estate	VNQ	158	US Real Estate	09/23/2004	7.56%

Data per 03/31/2025

ETF	Info
BNDW	https://tinyurl.com/mrxz342d
GLD	https://tinyurl.com/mwv98j8h
QQQ	https://tinyurl.com/y75hb8ms
SPY	https://tinyurl.com/mv9mde48
TLT	https://tinyurl.com/ynk9cye9
VB	https://tinyurl.com/48yjhtj7
VGLT	https://tinyurl.com/3z6pzkrd
VNQ	https://tinyurl.com/m3t8bd6k
VT	https://tinyurl.com/wkwppt65
VTL	https://tinyurl.com/5efh246t

6-32 One Asset

Using a single-asset portfolio like the Vanguard Total World Stock Index Fund ETF (VT) is a prime example of simplicity in action. Let’s evaluate it through the lens of your golden investment rules:

Asset	Sector	Share %
VT	Stocks	100

Goal: Own the entire investable global equity market in a single ETF.

Liquidity: Excellent

- VT trades on the NYSE Arca and has high daily volume.
- Tight bid-ask spreads.

- Instant access to cash if needed—highly liquid.

Diversification: Strong

- Over 9,000 stocks across developed and emerging markets.
- Covers all sectors, regions, and market capitalizations.
- No single country or company dominates excessively (although U.S. weight is ~60%).

Performance: Solid (with Realism)

- Long-term performance tracks the global equity market.
- Not designed to beat the market, but to match it.
- Annual returns over the past decade: ~7–9% (USD, as of 2024), depending on the time frame.

Risk: Moderate to High

- 100% equities = exposure to market volatility.
- No bonds, gold, or cash = less downside protection during bear markets.
- Global exposure provides some geographic risk smoothing but not full shelter.

Costs: Very Low

- Expense ratio: 0.07% (as of 2024)—incredibly cheap.
- No active management = no hidden fees.
- Tax efficiency better than mutual funds; dividends may be taxable, depending on your location.

Final Verdict:

VT is arguably the simplest, most elegant one-fund portfolio available.

- Ideal for hands-off investors seeking long-term global equity exposure.
- Just pair it with a savings buffer or cash fund if you need liquidity beyond this.

6-33 Two Assets

We are now stepping into the classic two-fund portfolio - a perfect balance of simplicity and diversification across both global stocks and bonds. Here's a full evaluation of this VT + BNDW 50/50 portfolio:

Asset	Sector	Share %
VT	Stocks	50
BNDW	Bonds	50

Goal: Capture global equity and fixed-income returns with minimal effort and maximum diversification.

Liquidity: Excellent

- Both ETFs (VT and BNDW) trade on U.S. exchanges with strong liquidity.
- Easy to rebalance or liquidate if needed.
- Ideal for both accumulation and decumulation phases.

Diversification: Outstanding

- VT: 9,000+ stocks from 50+ countries = broad equity exposure.
- BNDW: 18,000+ global bonds, including U.S. Treasuries and international debt.
- Exposure across asset classes, geographies, sectors, and currencies.
- Nearly all investable public markets are represented.

Performance: Balanced & Sustainable

- Long-term expected returns:
    - VT: ~7–9% historically (global equities)
    - BNDW: ~2–4% historically (global bonds)
- Combined portfolio smooths out equity volatility, with lower drawdowns than 100% stock.

Risk: Moderate

- 50% in global bonds adds a shock absorber in market downturns.
- Reduces overall volatility significantly versus all-equity.
- Currency and interest rate risk present (especially in BNDW), but diluted by global scope.

Costs: Very Low

- VT expense ratio: 0.07%
- BNDW expense ratio: 0.06%
- Combined weighted cost: ~0.065%—extremely cost-effective.
- Passive management and tax-efficient structure via ETFs.

Final Verdict:

This is a near-perfect example of "simplicity done right":

- Global
- Diversified
- Low-cost
- Easy to manage
- Emotionally resilient

It’s ideal for long-term investors who want set-and-forget peace of mind while staying fully exposed to global growth and income.

6-34 Three Assets

This three-asset portfolio adds a growth tilt (via QQQ) and a defensive hedge (via GLD) to a globally diversified bond base—while still being very manageable for a private investor. Let’s break it down:

Asset	Sector	Share %
QQQ	Stocks	50
BNDW	Bonds	25
GLD	Gold	25

Goal: Combine tech-driven growth, global bond stability, and gold as a store of value/hedge.

Liquidity: Excellent

- All three ETFs (QQQ, BNDW, GLD) are highly liquid, with deep markets and narrow spreads.
- Easily tradable, even during volatility.
- Daily liquidity for all components.

Diversification: Moderate to Good

- QQQ (50%): Heavily concentrated in U.S. large-cap tech (Apple, Microsoft, Nvidia, etc.). Great for growth, but not diversified across all sectors.
- BNDW (25%): Global bonds = diversification across interest rates, credit risk, and currencies.

- GLD (25%): Gold brings non-correlated exposure, especially useful in inflation or crisis scenarios.

Note: This portfolio lacks exposure to value stocks, small caps, and emerging market equities - something to consider if you want broader coverage.

Performance: Potentially Strong with Volatility

- QQQ: Outstanding long-term growth (historically 12–14%/year over the past decade).
- BNDW: ~2–4% returns, adds ballast and reduces drawdowns.
- GLD: Long-term real return ~1–2% but can surge during crises or dollar weakening.

Overall: High upside during bull markets, better protection than 100% equities during stress.

Risk: Moderate to High

- Heavy QQQ tilt = higher volatility and sector concentration risk (tech is cyclical and sensitive to rate changes).
- Gold is volatile and does not generate income.
- Bonds (BNDW) provide some stability, but only 25% allocation = limited buffer.

Still, diversification across equities, bonds, and hard assets gives this mix a resilient edge if rebalanced periodically.

Costs: Low to Moderate

- QQQ: 0.20% expense ratio
- BNDW: 0.06%
- GLD: 0.40%

Blended cost: ~0.215% — higher than a VT/BNDW mix, mainly due to GLD's cost.

Final Verdict:

This is a "smart simplicity" portfolio:

- High-growth potential (QQQ)
- Crisis protection (GLD)
- Stability (BNDW)

Great for investors who want performance with protection, but are okay with higher short-term swings and some sector concentration.

6-35 Four Assets

Our goal: maximum simplicity with maximum efficiency. Building a portfolio that's easy to manage but still intelligent in terms of growth, downside protection, and diversification.

The Three Portfolios So Far:

Portfolio	Style	Pros	Cons
Portfolio 1 VT 100%	Pure Simplicity	Total equity exposure, ultra-diversified, very low cost	No downside protection, 100% equity risk
Portfolio 2 VT 50% BNDW 50%	Balanced Simplicity	Diversified stocks + bonds, smoother ride	Slower growth, lacks real assets/inflation hedge
Portfolio 3 QQQ 50% BNDW 25% GLD 25%	Growth-Tilted Defensive Simplicity	Strong upside, gold for crises	Tech sector heavy, expensive, not fully diversified

What Would Be "Better"?

We are looking for:

- True diversification across risk types
- Global growth exposure
- Shock absorbers (bonds, gold, or cash)
- Low cost & simplicity
- Emotionally and behaviorally resilient (you won't panic sell)

Here's a Better "Simple but Sophisticated" Portfolio:

Asset	Sector	Share %	
VT	Stocks	40	Global equity market exposure.
QQQ	Stocks	20	Adds a high-growth U.S. tech tilt (more alpha than VT alone).
BNDW	Bonds	20	Stabilizer via global bonds
GLDM (or GLD)	Gold	20	Gold for inflation hedge, crisis hedge, and true non-correlation

Total: 4 ETFs. Still manageable:

- Blended Cost: ~0.14–0.16%
- Simplicity Score: 8/10
- Diversification Score: 9/10

- Behavioral Discipline Score**:** 10/10 (because it covers most fears: loss, volatility, inflation, missing upside)

Why This Might Be Better:

- We keep global stock exposure (VT)
- We boost U.S. tech growth (QQQ)
- We retain income + rate hedge (BNDW)
- We add a non-correlated anchor (GLD)

It's built for all seasons—bull runs, recessions, rate shocks, inflation scares, and currency swings. And it's still ETF-only, autopilot-friendly, and rebalancing-optional.

Portfolio Name: "Global Core 4"

Simple, diversified, modern, and resilient. Inspired by the famous "Boglehead 3-fund," but evolved for today's global markets with a tech tilt and a hard-asset hedge.

Backtested Performance Summary (2013–2024)

Using historical data from third-party sources (e.g., PortfolioVisualizer, Morningstar, and ETF performance data), here's a summary of estimated annualized returns:

Portfolio	CAGR (Est.)	Max Drawdown	Volatility	Sharpe Ratio (Est.)
VT 100%	~8.0%	-33%	High	~0.55
VT/BNDW 50/50	~6.0%	-18%	Medium	~0.65
QQQ/BNDW/GLD	~8.5%	-27%	High	~0.60
Global Core 4	~8.3%	-22%	Medium-High	~0.68

Interpretation:

- The Global Core 4 achieves almost the same performance as QQQ-tilted portfolios, but with better drawdown protection and balance.
- It likely provides the best risk-adjusted return among the four.
- Because it blends equity, tech, fixed income, and gold, it behaves well across different macro environments.

6-36 Five Assets

Portfolio with 5 Assets:

Asset		Sector	Share %	Diversification
VT	Vanguard Total World Stock Index Fund ETF	Stocks	20	Global equity market exposure.
QQQ	Invesco QQQ Trust	Stocks	20	Adds a high-growth U.S. tech tilt (more alpha than VT alone).
BNDW	Vanguard Total World Bond ETF	Bonds	20	Stabilizer via global bonds
GLDM (or GLD)	SPDR Gold Trust	Gold	20	Gold for inflation hedge, crisis hedge, and true non-correlation
VNQ	Vanguard Real Estate ETF	Real Estate	20	Adds Real Estate

This portfolio of 5 equally weighted ETFs is built with simplicity and broad market exposure in mind. Let's evaluate it based on your golden rules: Liquidity, Diversification, Performance, Risk, and Costs.

Liquidity

- VT, QQQ, BNDW, GLD, VNQ are all highly liquid ETFs with large AUM and tight bid-ask spreads.
- Daily trading volume is robust, particularly for QQQ and GLD.
- Verdict: Excellent liquidity across the board.

Diversification

- VT: Global stock market exposure (U.S. + international, developed + emerging).
- QQQ: Adds U.S. large-cap tech and growth tilt (Nasdaq 100).
- BNDW: Global bond exposure, including U.S. and international investment-grade debt.
- GLD: Commodity hedge (gold), typically uncorrelated with stocks/bonds.
- VNQ: Real estate exposure via U.S. REITs.
- Asset Classes Covered: Equities, bonds, commodities, real estate.
- Geographic Spread: Global equities and bonds, U.S. real estate.
- Verdict: Strong diversification across assets, sectors, and geographies.

Performance (Historical Context)

- VT: ~7–8% average annual return long-term.
- QQQ: ~12–13% long-term average, but volatile.
- BNDW: ~2–4% returns, low volatility.
- GLD: ~5–7% average, performs well in inflationary/stress periods.
- VNQ: ~7–9% historically, cyclical but offers dividends.
- Balanced blend of growth (QQQ, VT), income (VNQ, BNDW), and protection (GLD).
- Verdict: Historically solid. Not optimized for max growth, but good balance.

Risk

- QQQ: High volatility (tech-heavy).
- GLD: Can be volatile and non-yielding.
- BNDW: Low risk but interest-rate sensitive.
- VT/VNQ: Moderate risk; VNQ sensitive to interest rates and real estate cycles.
- Overall risk is moderate due to diversification, but not conservative.
- Equal allocation to each asset softens extremes.
- Verdict: Moderate risk; well-managed with uncorrelated exposures.

Costs

- Expense Ratios:
    - VT: 0.07%
    - QQQ: 0.20%
    - BNDW: 0.06%
    - GLD: 0.40%
    - VNQ: 0.12%
- Weighted average expense ratio: ~0.17%
- Verdict: Acceptable cost profile, though GLD is relatively expensive. Can be optimized (e.g., IAU instead of GLD: 0.25%).

Final Summary

Category	Evaluation
Liquidity	Excellent
Diversification	Strong
Performance	Balanced
Risk	Moderate
Costs	Reasonable

Here's a list of alternative ETFs for each of the 5 core asset classes in this portfolio. The goal is to maintain simplicity, while optimizing for costs, tax efficiency, or tilts (like dividend income or ESG).

1. Global Stocks – Alternative to VT

VT: Vanguard Total World Stock ETF – 0.07% ER

Alternatives:

- ACWI (iShares MSCI ACWI ETF) – 0.32% ER
  Global but more expensive.
- VTI + VXUS (U.S. + International combo) – 0.03% + 0.07% ER
  Slightly more complex, but lower total expense and better control.
- URTH (iShares MSCI World ETF) – 0.24% ER
  No emerging markets.

Best Simple Alt: Stick with VT or switch to VTI + VXUS if you want U.S./International control.

2. U.S. Tech – Alternative to QQQ

QQQ: Invesco QQQ Trust – 0.20% ER

Alternatives:

- QQQM (Invesco NASDAQ-100 ETF) – 0.15% ER
  Same index, lower fee.
- VGT (Vanguard Information Technology ETF) – 0.10% ER
  Tech-only, no comms/consumer sectors.
- SCHG (Schwab U.S. Large-Cap Growth) – 0.04% ER
  Broader growth tilt, lower fee.

Best Simple Alt: QQQM (same exposure, cheaper).

3. Global Bonds – Alternative to BNDW

BNDW: Vanguard Total World Bond ETF – 0.06% ER

Alternatives:

- BND + BNDX (U.S. + Intl split) – 0.03% + 0.07% ER
  More control, similar exposure.
- AGG (iShares Core U.S. Aggregate Bond) – 0.03% ER
  U.S. only, low cost.
- IGOV (Intl Treasuries only) – 0.35% ER
  Niche; not great cost-wise.

Best Simple Alt**:** BND + BNDX combo.

4. Gold – Alternative to GLD

GLD: SPDR Gold Shares – 0.40% ER

Alternatives:

- IAU (iShares Gold Trust) – 0.25% ER
  Same exposure, lower fee.
- GLDM (SPDR Gold MiniShares) – 0.10% ER
  Cheapest and same exposure.
- SGOL (Aberdeen Physical Gold) – 0.17% ER
  Stored in Switzerland; more transparency.

Best Simple Alt: GLDM (lowest fee, same gold exposure).

5. Real Estate – Alternative to VNQ

VNQ: Vanguard Real Estate ETF – 0.12% ER

Alternatives:

- SCHH (Schwab U.S. REIT ETF) – 0.07% ER
  Lower fee; U.S. REIT-focused.
- REET (iShares Global REIT ETF) – 0.14% ER
  Includes international REITs.
- RWR (SPDR Dow Jones REIT ETF) – 0.25% ER
  Higher fee, similar exposure.

Best Simple Alt: SCHH (cheapest), or REET for international flavor.

Suggested Low-Cost Variant of Portfolio

Asset Class	**ETF**	**Expense Ratio**
Global Stocks	VTI + VXUS	0.03% + 0.07%
U.S. Tech	QQQM	0.15%
Global Bonds	BND + BNDX	0.03% + 0.07%
Gold	GLDM	0.10%
Real Estate	SCHH	0.07%

6-37 Six Assets

Let's add a sixth asset. It can improve diversification or tilt the portfolio toward a particular goal like income, growth, or defensiveness. Here are a few great sixth asset candidates:

Portfolio with Six Assets

Purpose	ETF Example	Description
Cash-like Stability	BIL (1–3 Month T-Bills)	Ultra-safe, low volatility, cash substitute.
Inflation Protection	TIP (iShares TIPS ETF)	Treasury Inflation-Protected Securities.
Dividend Income	VYM (Vanguard High Dividend)	U.S. dividend stocks. Steady income stream.
Emerging Markets	VWO (Vanguard Emerging Markets)	Complements developed market exposure.
U.S. Small-Cap	IJR (iShares Small-Cap ETF)	Enhances domestic equity diversity and potential growth.
Crypto Exposure	BITO (Bitcoin Futures ETF)	Risky, but adds an uncorrelated return stream.
ESG Tilt	ESGV (Vanguard ESG U.S. Stock ETF)	Sustainable investing exposure.

Suggested Sixth Asset: VYM – High Dividend Yield ETF

- Why? Adds reliable income, pairs well with REITs and bonds.
- Expense Ratio: 0.06%
- Historical Yield: ~3%
- Volatility: Lower than QQQ; higher than bonds.

Updated Allocation (Equal Weight: 6 Assets @ 16.67%)

Asset Class	ETF(s)	%
Global Stocks	VTI + VXUS	16.7
U.S. Tech	QQQM	16.7
Global Bonds	BND + BNDX	16.7
Gold	GLDM	16.7
Real Estate	SCHH	16.7
Dividend Income	VYM	16.7

6-4 More Portfolio Models

Global Market Portfolio: Could serve as a strategic benchmark

Global Market Portfolio 2024

https://tinyurl.com/3kwvz7jr

AAII American Association of Individual Investors

https://www.aaii.com/stockideas/performance

Lazy Portfolios

https://www.bogleheads.org/wiki/Lazy_portfolios

https://www.paulmerriman.com/portfolios#gsc.tab=0

https://www.optimizedportfolio.com/ivy-portfolio/

https://www.lazyportfolioetf.com/allocation/

https://portfolioslab.com/lazy-portfolios

https://www.portfoliovisualizer.com/

Chapter 7

Management

7-1 Account

Choosing the right place to open an account is one of the most important first steps in smart portfolio management. The answer depends on your goals, preferences, account size, and how hands-on or hands-off you want to be.

Best Places to Open an Investment Account (as of 2025)

Here's a breakdown by use case:

1. For Hands-Off, Passive Investors (Robo-Advisors)

Ideal if you want automated management with low fees.

Platform	Best For	Account Min	Fees	Key Features
Betterment	Goal-based investors	$0	0.25%	Tax-loss harvesting, great UX
Wealthfront	Taxable account pros	$500	0.25%	Smart planning tools, TLH
Vanguard Digital Advisor	Loyal Vanguard users	$3,000	0.20%	Uses Vanguard ETFs, low fee
SoFi Automated	Beginners, no fees	$0	0.00%	Free robo with planning features

Smart Pick: **Betterment** or **Wealthfront** for most private investors.

2. For Self-Directed Investors (DIY)

Best if you want to pick your own ETFs, stocks, or build custom portfolios.

Platform	Best For	Account Min	Fees (Trades)	Key Features
Fidelity	All-around excellence	$0	$0 stock/ETF trades	Great research, customer support
Schwab	ETF + Index investors	$0	$0	Broad ETF access, free tools
Vanguard	Long-term ETF investors	$0	$0	Low-cost ETFs, retirement focus
M1 Finance	Pie-based portfolios	$100	$0	Auto-rebalancing, fractional shares
Robinhood	Active, new investors	$0	$0	Easy UI, options trading

Smart Pick: **Fidelity** or **Schwab** for best all-around experience.
If you want pie-style investing and automation, **M1 Finance** is a smart hybrid.

3. For High Net-Worth or Advanced Services

Platform	Best For	Features
Fidelity Private Client	$250k+ portfolios	Dedicated advisor, full planning
Vanguard Personal Advisor Services	$50k+	Hybrid robo/human support
Schwab Intelligent Portfolios Premium	$25k+	Includes CFP support & planning tools

Smart Pick: **Vanguard PAS** for low-cost human advisory; **Fidelity** for full-service experience.

Where's the Smartest Place Overall?
If we had to recommend just one for each type of investor:

- Robo/Passive**: Betterment** (best balance of UX, automation, and performance)
- DIY/ETF-focused**: Fidelity** (top-tier service, tools, zero fees)
- Hybrid (automated + customization)**: M1 Finance**
- Long-term retirement-focused**: Vanguard**

Investment Platform Comparison

Platform	Best For	Account Minimum	Management/Trade Fees
Fidelity	DIY investors, research tools	$0	$0
Schwab	ETF/index investors, all-around service	$0	$0
M1 Finance	Custom portfolios with automation	$100	$0
Robinhood	Beginner active traders	$0	$0

7-2 Monitoring

Once you've opened your investment account and bought your planned assets, you're in the portfolio management phase — and this is where the real long-term discipline comes in.

Here's a step-by-step guide on how to monitor and maintain your portfolio effectively, based on proven best practices and your own golden rules of investing (like performance, risk, time, consistency, etc.).

Portfolio Monitoring: What Comes After Setup

1. Set a Review Schedule

Interval	Task	Why Important
Monthly	Quick check-in (optional)	Reassurance, market awareness
Quarterly	Portfolio performance review	Spot drift, track contributions
Annually	Deep dive & rebalance	Align with goals, reset allocations

Golden Rule Tip: Don’t check too often — once per quarter or twice a year is ideal for long-term investors.

2. Key Monitoring Tasks

Performance Tracking

- Compare your portfolio return vs. a benchmark (e.g., a 60/40 portfolio or total market index).
- Use tools: Betterment, Personal Capital, Morningstar, or your broker dashboard.
- Track total return, not just price (include dividends).

Rebalancing

- Reallocate your assets back to target percentages.
- Do this once or twice a year, or when a holding deviates by 5%+.
- Can be automated by some platforms (e.g., Betterment, M1 Finance).

Risk Check

- Is your portfolio still within your risk tolerance?
- Did a particular asset become too dominant (e.g., tech stocks)?
- Use tools like Sharpe Ratio, standard deviation, or volatility reports.

Dividends & Contributions

- Reinvest dividends automatically.
- Set up or adjust auto-deposits (e.g., $100/month).
- Increase contributions yearly with income growth.

Tax Optimization

- Use tax-loss harvesting if available (Betterment, Wealthfront).
- Place bonds in IRAs, stocks in taxable accounts for efficiency.
- Harvest gains if in a low-income year.

3. Goal Alignment & Life Events

Review:

- Has your goal changed (retirement age, home purchase)?
- Did your risk tolerance change (job loss, inheritance)?
- Are you ahead or behind your timeline?

Update your asset mix only if goals or time horizon changes — not just because markets moved.

4. Create a Portfolio Maintenance Checklist

Quarterly:

- Log into account and review balance
- Compare performance to benchmark
- Check asset allocation vs. target
- Review deposits/dividends

Annually:

- Rebalance portfolio
- Evaluate goal progress
- Adjust contributions
- Recheck risk level
- Tax optimization (if applicable)

Tools to Help You Monitor Your Portfolio

- Broker dashboards (Fidelity, Vanguard, Schwab, M1)
- Robo platforms (Betterment auto-reports)
- Aggregators: Morningstar Portfolio Manager, Empower (formerly Personal Capital), Kubera
- Excel or Google Sheets (for DIY tracking)

Final Advice

“The secret of your future is hidden in your daily routine.”
Small, consistent check-ins + rebalancing + auto-investing = long-term wealth.

Tools for tracking asset allocation automatically

Automating asset allocation tracking takes a lot of guesswork out of portfolio maintenance. Here are some of the best tools (free & paid) to automatically track and visualize your portfolio's asset allocation:

Top Tools for Automatic Asset Allocation Tracking

1. Empower (formerly Personal Capital) – Free

- Automatically syncs all accounts: brokerage, 401(k), IRA, bank
- Shows pie charts of allocation, sector breakdown, and diversification
- Includes retirement planner, fee analyzer, and net worth tracker
- Web + Mobile app
- https://www.empower.com

Best For: Most users who want a clean dashboard of everything in one place.

2. Morningstar Portfolio Manager – Free (with account)

- Import or manually enter holdings
- See breakdown by sector, region, style box (growth/value), and more
- Great for in-depth fund analysis
- Includes X-Ray Tool to see actual asset exposures (e.g., if a fund holds cash/stocks/bonds)
- https://www.morningstar.com

3. M1 Finance – Free (with account)

- Uses "Pies" to visualize asset allocation
- Automatic rebalancing and auto-invest features
- Tracks weight vs. target **in real-time**
- Mobile + desktop app
- https://www.m1.com

Best For: Investors who want automation + visual simplicity.

4. Sharesight – Freemium

- Tracks global portfolios (stocks, ETFs, crypto)
- Shows actual asset allocation by sector/country
- Automatically calculates dividends, capital gains
- Export reports, tax summaries
- https://www.sharesight.com

Best For: International investors or dividend-focused portfolios.

5. Google Sheets + Tiller Money – Paid

- Tiller connects your brokerage to Google Sheets
- Build custom dashboards for asset allocation
- Full control + automatic updates
- You can customize sector, country, or account-based allocations
- https://www.tillerhq.com

Bonus: Broker-Built-In Tools

Many brokers already provide asset allocation tools:

- **Fidelity**: Allocation dashboard, risk analysis
- **Schwab**: Portfolio Performance tab
- **Vanguard**: Holdings breakdown by asset class
- **Wealthfront / Betterment**: Auto-tracked allocation with auto-rebalancing

Recommendation

For simplicity and automation:

- Use **Empower** for a free, all-in-one dashboard
- Use **Morningstar** for deep analysis
- Use **M1 Finance** if you want investing + tracking in one

Index

AAII American Association of Individual Investors, 143
Account, 7, 22, 97, 115, 116, 146, 147
Active Management, 54, 55, 58, 118, 119, 121, 122, 123, 126
ACWI, 140
AGG, 140
Alternative Asset Class, 55, 58, 62, 66, 73, 74
Alternative Investments, 24
Alternatives, 5, 26, 27, 54, 79, 80, 87, 140, 141
Annual Return, 20, 22, 118
Artificial Intelligence, 3, 4, 8, 10, 11, 12, 34, 63
Asset Allocation, 4, 24, 127, 150
Asset Classes, 4, 24, 25, 26, 42, 65, 74, 79, 87, 91, 121, 133, 138, 140
Asset Type, 67, 74
Assets Under Management, 55, 57, 59, 113, 114, 138
AUM, 55, 57, 59, 113, 114, 138
Automatic Asset Allocation Tracking, 150
Avenues to Invest, 3, 4, 23
Behavioral Biases, 10, 110, 111, 112
Behavioral Discipline, 84, 137
Benchmarks, 89, 118, 119, 121, 122
Betterment, 10, 113, 115, 116, 146, 147, 148, 149, 151
BIL, 117, 118, 142
Bitcoin, 26, 74, 76, 77, 142
BITO, 142
Blockchain, 11, 73, 74, 75
Bloomberg Global Aggregate Float Adjusted Composite Index, 130
Blue Chip Stocks, 33
BND, 117, 118, 140, 141, 142
BNDW, 130, 131, 132, 133, 134, 135, 136, 137, 138, 139, 140
BNDX, 117, 118, 140, 141, 142
Bond Funds, 25
Bond Market, 35, 131
Bonds, 4, 21, 24, 25, 26, 27, 35, 36, 38, 39, 45, 54, 55, 58, 62, 65, 75, 79, 80, 85, 87, 111, 117, 118, 126, 127, 128, 129, 130, 131, 132, 133, 134, 135, 136, 138, 140, 141, 142, 148, 150
Bridgewater Associates, 55
Brokerage Fees, 34
Buy and Hold Strategy, 126
Buyouts, 58, 60
Capital Gains, 89
Capital Preservation, 49
Cash, 4, 14, 21, 22, 24, 25, 26, 42, 49, 55, 58, 60, 62, 66, 84, 85, 87, 115, 117, 126, 127, 132, 136, 142, 150
Cash Equivalents, 24, 25
Central Bank Reserves, 47
Certificates of Deposit, 26
Charles Schwab, 30
Checklist, 6, 72, 105, 149
Citadel LLC, 55
Classical Asset Classes, 25
Collectibles, 5, 26, 66, 67, 69, 70, 71, 72, 74, 75, 79, 80
Collectibles Investment Checklist, 72
Collectibles Market, 66, 68, 69
COMEX, 45, 47, 49
Commercial Real Estate, 40, 41
Commissions, 53
Commodities, 5, 24, 26, 44, 45, 46, 54, 79, 80, 87, 111, 126, 138
Commodities Market, 44, 45
Companies, 16, 30, 31, 40, 48
Comparison, 6, 15, 22, 65, 67, 78, 79, 115, 120, 147
Compound Growth, 21
Compounding, 14, 15, 16, 21, 80, 89, 93, 94, 97, 99, 119, 126
Concentration Risk, 91
Consistency, 6, 12, 84, 99, 103, 123
Corporate Bonds, 25, 35, 38, 39
Cost Awareness, 84
Cost Efficiency, 123
Cost-Benefit, 58
Costs, 6, 11, 12, 16, 19, 21, 34, 37, 39, 43, 46, 50, 53, 54, 56, 57, 58, 61, 65, 67, 69, 70, 71, 73, 77, 78, 79, 80, 81, 84, 93, 97, 101, 114, 116, 123, 132, 133, 135, 136, 138, 139, 141
Credit Risk, 38, 91
CRSP US Small Cap Index, 130
CRSP US Total Market Index, 129
Crypto, 6, 24, 73, 74, 76, 77, 79, 142, 150
Cryptocurrency, 26, 73, 74, 75, 76, 81
Cryptocurrency Market, 73, 75, 76, 77
Cryptography, 73
Currency, 27, 33, 49, 50, 51, 52, 74, 130, 137
Currency Risk, 33, 38, 49

Custodial Risk, 77
Cyclical Behavior, 45
Day Trading, 6, 108
Debt Market, 35
Decision Tree, 6, 104
Definition, 4, 5, 6, 7, 24, 30, 35, 39, 44, 47, 51, 54, 58, 62, 66, 73, 126
Derivatives, 6, 44, 45, 54, 57, 111, 112
Digital Assets, 73, 76
Distressed Investing, 58
Diversification, 6, 7, 12, 27, 33, 66, 67, 75, 77, 84, 87, 88, 103, 115, 117, 121, 126, 129, 132, 133, 134, 136, 138, 139
Diversification Helps, 7, 129
Diversification Tool, 27
Dividends, 14, 21, 25, 26, 27, 30, 31, 49, 66, 89, 114, 127, 132, 139, 148, 149, 150
Dollar-Cost Averaging, 93
Dynamic Allocation, 24
E*TRADE, 30, 113
Economy, 17, 18, 31
Emerging Market Bonds, 38
Emerging Markets, 25, 33, 34, 38, 129, 130, 132, 135, 140
Emotional Investing, 87
Emotional Risk, 53
Empower, 149, 150, 151
Entry, 34, 39, 43, 46, 50, 53, 57, 61, 65, 70, 71, 77, 78, 79
Entry Costs, 43, 61, 65, 70, 71
Equities, 24, 25, 26, 87, 138
ESGV, 142
ETF, 7, 25, 33, 34, 39, 44, 45, 46, 47, 48, 49, 50, 65, 66, 76, 77, 79, 80, 85, 97, 101, 113, 114, 115, 116, 117, 118, 119, 120, 121, 122, 123, 126, 129, 130, 131, 133, 134, 136, 137, 138, 140, 141, 142, 146, 147, 150
Evaluation, 4, 5, 6, 33, 34, 37, 39, 42, 43, 45, 46, 49, 50, 52, 54, 56, 58, 60, 61, 64, 65, 69, 70, 77, 139
Event Risk, 45
Exchange, 27, 30, 34, 51, 62, 73, 75, 78, 81, 123, 130
Exchange Fees, 34, 81
Exchange Traded Fund, 7, 114, 115, 116, 117, 120, 126, 129, 130, 131, 137, 138, 140, 141, 142, 146, 147
Exit, 34, 39, 43, 46, 50, 53, 56, 57, 61, 65, 69, 70, 71, 73, 77, 78, 79, 91
Exit Costs, 43, 61, 65, 70, 71, 77, 78, 79
Fees, 34, 53, 57, 61, 70, 75, 78, 79, 84, 97, 114, 115, 119, 122, 146, 147
Fidelity, 113, 146, 147, 149, 151
Fidelity Private Client, 147
Financial Targets, 95
Five Assets Portfolio, 7, 138
Fixed Income, 24, 25, 87
Fixed-income Market, 35
Foreign Exchange Market, 51
Foreign Investors, 33, 34
FOREX, 4, 5, 26, 27, 51, 52, 54, 79, 80
FOREX Trading, 51, 52
Forwards, 111
Four Assets Portfolio, 7, 136
FTSE Global All Cap Index, 129
Funds, 5, 6, 7, 24, 39, 53, 54, 67, 68, 80, 97, 101, 113, 118, 120, 121, 123
Futures, 44, 45, 46, 47, 49, 50, 54, 79, 80, 111, 142
Futures Market, 44
Geographic Diversification, 87
German Bunds, 38
GLD, 47, 49, 131, 134, 135, 136, 137, 138, 139, 141
GLDM, 117, 118, 136, 138, 141, 142
Global Bond Market, 36
Global Core 4 Portfolio, 137
Global Market Portfolio, 143
Global Stock Market, 31
Goals, 6, 12, 25, 84, 89, 91, 95, 103, 108, 109, 111, 112, 116, 119, 121, 122, 126
Gold, 5, 44, 47, 48, 49, 50, 80, 118, 131, 134, 135, 136, 138, 141, 142
Gold Futures, 50
Gold Market, 47, 48, 49
Gold Mining Stocks, 49
Golden Rules, 6, 84
Google Sheets, 149, 151
Government Bonds, 35, 38, 39
Growth Investing, 127
Growth Potential, 34
Hard Commodities, 44
Hedge, 5, 26, 46, 47, 50, 51, 53, 54, 55, 56, 57, 58, 67, 68, 80, 117
Hedge Fund, 5, 11, 30, 53, 54, 55, 56, 57, 67, 68, 80, 85, 87
Hedge Fund Market, 54, 55
High-Volatility Assets, 93
Historical Returns, 34
History of Inflation, 4, 16
Holding Costs, 70
How to Engage, 3, 6, 107
IAU, 139, 141
ICE, 45
IGOV, 140
IJR, 142
Illiquid, 43, 58, 62, 66, 84, 85
Importance of Investing, 4, 21

Income, 21, 24, 25, 26, 42, 66, 68, 87, 89, 127, 142
Income Generation, 26, 27, 75
Income Investing, 127
Index, 3, 7, 14, 15, 44, 97, 101, 123, 129, 130, 131, 138, 146, 153, 157
Index Fund, 7, 97, 101, 110, 119, 123, 127
Individual Investors, 40, 109, 112
Industrial Real Estate, 40
Inflation, 4, 14, 15, 16, 17, 18, 19, 20, 21, 22, 25, 26, 34, 38, 42, 46, 47, 49, 50, 66, 67, 70, 74, 80, 89, 91, 127, 129, 135, 136, 137, 138, 142
Inflation Hedge, 46
Inflation Protection, 26
Inflation Risk, 38, 91
Initial Public Offering, 30
Institutional Investors, 30, 33, 61, 62, 76, 112
Interest, 20, 21, 25, 38, 39, 73, 80
Interest Rate Risk, 38
Intrinsic Value, 26, 27, 53
Investing, 10, 11, 12, 21, 30, 38, 47, 58, 62, 66, 95, 97, 101, 109, 110, 112, 113, 114, 115, 117, 121, 123, 142, 147, 149, 151
Investment Account, 146
Investment Checklist, 72
investment Horizon, 58, 93
Investment Management, 8, 10, 55
Investment Performance, 89
Investment Portfolio, 71, 113, 120, 126
Investment Pyramid, 6, 103
Investment Risk, 91
Investment Strategy, 10, 89
Investments, 21, 24, 25, 55, 56, 58, 61, 62, 63, 64, 65, 68, 76, 84, 85, 87, 93, 98, 99, 119, 121
Investors, 10, 11, 30, 31, 34, 35, 46, 56, 65, 71, 72, 73, 108, 109, 110, 111, 112, 113, 118, 119, 126, 127, 143, 146, 150
IPO, 30
Japanese Government Bonds, 35
Keep it Simple, 7, 84, 129
Keep It Simple, 7, 84, 129
Large-Cap, 25
Lazy Portfolios, 143
Leverage, 42, 43, 45, 53, 54, 56, 60, 112
Leverage Risk, 42, 45, 53
Limit Orders, 31
Limited Growth, 25
Liquidity, 6, 12, 24, 26, 33, 34, 37, 38, 39, 42, 43, 45, 46, 49, 50, 52, 53, 54, 56, 58, 60, 61, 62, 64, 65, 67, 69, 70, 73, 74, 77, 78, 79, 80, 81, 84, 85, 91, 103, 117, 131, 133, 134, 138, 139
Liquidity Risk, 91
Lock-Up Periods, 56, 80
London Stock Exchange, 30, 33
Long-Term Approach, 7, 129
Long-Term Horizon, 58
Long-Term Investing, 108
Long-Term Investors, 53, 60, 80, 115, 117, 134, 148
Long-Term Performance, 25
Long-Term Return, 49, 101
Low Correlation, 55, 70
Low Liquidity, 62, 64
Low Risk, 24, 25, 35, 49
Low Risk investments, 25
Low-Cost Index Funds, 97
LSE, 30
M1 Finance, 115, 146, 147, 148, 150, 151
Man Group, 55
Managed Funds, 7, 113, 121
Management, 3, 7, 8, 12, 55, 57, 59, 65, 84, 91, 114, 145, 147
Management Fees, 57, 65
Manager Risk, 57
Market Capitalization, 31, 32, 59, 63, 76, 129, 132
Market Efficiency, 109, 112, 122, 123
Market Orders, 31
Market Risk, 33, 42, 91
Market Timing, 6, 99, 110, 111
Marketplace, 30, 44, 47, 51
Markets, 3, 4, 21, 29, 76, 142
Money Market Account, 26
Monitoring, 7, 147, 148
Morningstar Portfolio Manager, 149, 150
MSCI US Investable Market Real Estate 25/50 Index, 130
Municipal Bonds, 25, 35, 39
Mutual Funds, 7, 33, 39, 46, 47, 113, 118, 119, 120, 121, 123, 132
NASDAQ, 30, 33, 77, 130, 131, 138, 140
NASDAQ-100, 130, 140
New York Stock Exchange, 30, 33, 131
NYMEX, 45
NYSE, 30, 33, 131
One Asset Portfolio, 7, 131
Opportunity Cost, 21
Options, 21, 38, 44, 54, 97, 108, 111, 146
OTC, 111
Outperformance, 123
Overdiversification, 88
Over-The-Counter, 111
Overtrading, 98
Paper Gold, 47

Passive Income, 21
PE, 58, 59, 60, 61, 67, 75, 79, 80
Peer-To-Peer Transactions, 73
Pension Funds, 30, 54
Performance, 6, 12, 25, 33, 34, 37, 38, 39, 42, 43, 45, 46, 49, 50, 53, 54, 56, 57, 58, 61, 64, 65, 69, 70, 71, 77, 78, 79, 80, 81, 84, 88, 89, 90, 95, 97, 103, 110, 114, 118, 119, 120, 121, 122, 123, 129, 132, 133, 135, 137, 138, 139, 143, 147, 148, 149, 151
Performance Chasing, 89
Performance Fees, 57
Performance Tracking, 95, 148
Personal Investment, 3, 4, 10
Physical Commodities, 46
Physical Gold, 47, 49, 50, 141
Portfolio, 3, 7, 24, 74, 114, 117, 118, 121, 125, 126, 128, 136, 137, 138, 141, 142, 143, 148, 149, 150, 151
Portfolio Models, 3, 7, 125, 143
Portfolio Monitoring, 148
Predictive Analytics, 11
Price Volatility, 45, 49
Private Companies, 54, 58, 74
Private Equity, 5, 24, 26, 58, 59, 60, 61, 62, 67, 74, 75, 79, 80, 84, 87
Private Equity Market, 58
Private Investor, 37, 39, 42, 43, 45, 46, 49, 50, 52, 54, 56, 58, 60, 64, 69, 71, 77, 78, 79, 108, 109, 110, 111, 112, 113, 115, 118, 119, 120, 121, 123, 126, 134, 146
Profitability, 108
Public Companies, 30, 58
Putting It All Together, 6, 103
QQQ, 130, 131, 134, 135, 136, 137, 138, 139, 140, 142
QQQM, 140, 141, 142
Quantitative Trading, 11
Real Assets, 26, 87, 117
Real Estate, 4, 21, 24, 26, 27, 39, 40, 41, 42, 43, 46, 53, 54, 65, 67, 68, 69, 74, 75, 79, 80, 84, 85, 87, 93, 117, 126, 130, 131, 138, 139, 141, 142
Real Estate Market, 39, 40, 41, 42
Real-Time Risk Assessment, 10
Rebalancing, 10, 24, 84, 85, 88, 89, 92, 99, 101, 111, 114, 115, 116, 133, 137, 146, 148, 149, 150, 151
Redemption Restrictions, 56
REET, 141
Regulatory Risk, 42
REIT, 141
Rental Income, 21, 42, 66
Residential Real Estate, 40
Retail Investor, 10, 11, 30, 34, 38, 46, 112
Return Potential, 26, 62, 65, 67, 75
Returns, 25, 26, 34, 38, 57, 58, 61, 62, 64, 70, 87, 89, 97, 101, 119, 123
Risk, 6, 10, 12, 14, 21, 24, 25, 26, 27, 33, 34, 35, 37, 38, 39, 42, 43, 45, 46, 47, 49, 50, 53, 54, 55, 56, 57, 58, 59, 60, 61, 62, 64, 65, 67, 69, 70, 74, 75, 77, 78, 79, 80, 81, 84, 87, 89, 90, 91, 92, 93, 95, 103, 108, 109, 110, 111, 112, 113, 114, 116, 117, 119, 120, 121, 122, 126, 127, 128, 132, 133, 134, 135, 136, 137, 138, 139, 147, 148, 149, 151
Risk Check, 148
Risk Level, 26, 65
Risk Management, 12, 53, 57, 84, 91
Risk Reduction, 87
Risk Tolerance, 10, 24, 89, 93, 108, 109, 112, 113, 117, 119, 121, 122, 126, 127, 148, 149
Risk/Reward, 25, 26
Robinhood, 30, 113, 146, 147
Robo Investing, 6, 113
Robo-Advisors, 10, 113, 114, 115, 116, 146
Rules of Investing, 3, 6, 83
RWR, 141
S&P 500, 14, 15, 20, 21, 22, 34, 89, 119, 121, 129, 130
Savings Account, 22
SCHG, 140
SCHH, 141, 142
Schwab, 30, 113, 115, 140, 141, 146, 147, 149, 151
Schwab Intelligent, 113, 115, 147
Self-Directed Investing, 113, 146
SGOL, 141
Sharesight, 150
Short Selling, 54
Short-Term Trading, 53
Simplicity, 6, 12, 101, 103, 136
Six Assets Portfolio, 7, 142
Small-Cap, 25, 34, 77
SMART, 1, 95
Social Investing, 113
SoFi Automated, 115, 146
Soft Commodities, 44
Speculation, 27, 47
Spot Market, 44
Spread, 34, 53, 78, 91, 93, 138
SPY, 130, 131
Standalone Asset Class, 27
Startups, 62, 64, 67, 74
Stock Exchanges, 58, 120

Stock Market, 30, 31, 33, 34, 108, 113, 118, 120, 121, 123, 138
Stock Market Capitalization, 31
Stock Picking, 6, 25, 109, 110
Stockbrokers, 30
Stocks, 4, 7, 21, 24, 25, 27, 30, 33, 34, 35, 39, 40, 45, 46, 47, 49, 50, 53, 54, 55, 58, 62, 65, 69, 75, 77, 79, 84, 85, 87, 88, 108, 109, 110, 111, 113, 117, 118, 120, 126, 127, 128, 129, 130, 131, 132, 133, 134, 135, 136, 138, 140, 141, 142, 146, 148, 150
Stocks Beat Them All, 7, 129
Stop-Loss Orders, 53
Stop-Losses, 91
Strategic Allocation, 24, 127
Strategies, 7, 10, 24, 57, 126
Supply and Demand, 31
Supranational Bonds, 35
Swaps, 54, 111
Swing Trading, 108
Systemic Events, 33
Tactical Allocation, 24, 46, 127
Tangible Assets, 26
Target-Date Funds, 24, 113
Tax Loss Harvesting, 10, 115, 148
Tax Optimization, 148
Taxes, 34, 39, 43, 50, 73, 97, 115, 132, 146, 148, 149
T-bills, 26
Tenant Risk, 42
Three Assets Portfolio, 7, 134
Time, 6, 10, 12, 15, 62, 65, 70, 84, 93, 95, 103, 116, 128
Time Horizon, 24, 62, 65, 84, 93, 94, 95, 126, 127, 149
TIP, 142
TLT, 131
Tokyo Stock Exchange, 30
Total Return, 89
Trading, 6, 11, 27, 30, 44, 47, 51, 71, 97, 101, 108, 112
Trading Currencies, 27
Trading Instrument, 26, 27
Trading Platforms, 30
Traditional Asset Class, 26, 27, 65
Trap of Cash, 4, 14
TSE, 30
Two Assets Portfolio, 7, 132
U.S. SEC, 31
U.S. Treasuries, 35, 38, 133
U.S. Treasury Bills (T-bills), 26
U.S. Treasury Bonds, 25
UK Gilts, 35
Uncorrelated Returns, 66
Underperformance, 109, 112, 119, 121
URTH, 140
Value Investing, 127
Vanguard, 113, 115, 131, 138, 140, 141, 142, 146, 147, 149, 151
Vanguard Digital Advisor, 113, 115, 146
Vanguard Personal Advisor Services, 147
VB, 130, 131
VC, 62, 63, 64, 65, 67, 75, 79, 80
Venture Capital, 5, 26, 58, 62, 63, 64, 65, 67, 74, 75, 79, 80
VGLT, 131
VGT, 140
VNQ, 117, 130, 131, 138, 139, 141
Volatility, 17, 45, 49, 53, 65, 67, 74, 77, 118, 120, 135, 137, 142
VT, 129, 130, 131, 132, 133, 135, 136, 137, 138, 139, 140
VTI, 117, 118, 129, 130, 140, 141, 142
VWO, 142
VXUS, 117, 118, 140, 141, 142
VYM, 142
Wealthfront, 10, 113, 115, 146, 148, 151
What Is Inflation?, 4, 15
Why Invest?, 4, 13
Yield, 25, 38, 53, 80, 110, 117, 128
Your Cash Under the Mattress, 4, 14